Supreme Court, U.S.
FILED
NOV 23 2010
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William K. Suter, Clerk

No. 10-695

In The
Supreme Court of the United States

MARK D. LAY,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

Petition For A Writ Of Certiorari To The United States Court of Appeals For The Sixth Circuit

PETITION FOR A WRIT OF CERTIORARI
with Appendix

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November, 2010

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QUESTIONS PRESENTED

1. Do investment advisers to hedge funds owe fiduciary duties to investors in the funds?

2. Can the offenses of mail and wire fraud be committed in circumstances where there is no "gain" of any nature to the defendant nor use of the mail or wires to cause a person to part with money or property?

3. Was it reversible error for the trial court to fail to give a proper limiting instruction to the jury in connection with the use at Petitioner's trial of transcript testimony from an earlier deposition?

PARTIES

Petitioner, Mark D. Lay, was defendant in the trial court. Mr. Lay, a registered investment adviser, was convicted under federal mail and wire fraud and investment adviser fraud statutes for losses experienced by a hedge fund he managed, MDL Active Duration Fund (hereinafter "ADF"), into which the Ohio Bureau of Worker's Compensation (hereinafter "OBWC") unlawfully invested and lost $216,000,000.00[1]. There were no allegations that Petitioner profited financially or personally benefited from these losses. This appeal is about losses in the bond market. There was no theft, embezzlement or other gain to Petitioner.

Respondent is the United States of America.

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[1]The evidence at trial indicated that OBWC did not obtain authority to invest into hedge funds until 2004, a point in time subsequent to the initial investments here. OBWC invested $100M on August 20, 2003 and a second $100M on May 21, 2004. Hedge Fund investments were not approved by the OBWC Oversight Commission until August 2004.

TABLE OF CONTENTS

QUESTIONS PRESENTED 1

PARTIES 2

TABLE OF CONTENTS 3

TABLE OF AUTHORITIES 4

OPINIONS BELOW 2

JURISDICTION 2

CONSTITUTIONAL PROVISIONS 3

STATEMENT OF THE CASE 3
A. STATEMENT OF FACTS 3
1. DURATION AND LEVERAGE 9
B. COURSE OF PROCEEDINGS 12

REASON FOR GRANTING THE PETITION . . 14
a. Investment Adviser's Act and *Goldstein* 14
b. Fiduciary Relationship 20
c. Wire Fraud and Mail Fraud 35
d. The Sixth Circuit Failed To Follow *Skilling* . 42
e. Limiting Instructions 48

CONCLUSION 49

APPENDIX

TABLE OF AUTHORITIES

Cases

Am. Bar Ass'n v. FTC,
368 U.S. App. D.C. 368,
430 F.3d 457 (D.C. Cir. 2005) 35

Aschinger v. Columbus Showcase Co.,
934 F.2d 1402 (6th Cir. 1991) 21

Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.,
467 U.S. 837 (1984) 23, 25

Goldstein v. SEC,
451 F. 3d 873 (D.C. Cir. 2006) ..... *passim*

McNally v. United States,
483 U. S. 350 (1987) 43

Rewis v. United States,
401 U.S. 808 (1971) 45

SEC v. Capital Gains Research Bureau,
375 U.S. 180 (1963) 15

SEC v. North Shore Asset Management,
2008 U.S. Dist. LEXIS 36160
(S.D. NY May 5, 2008) 14

SEC v. Trabluse,
526 F. Supp.2d 1008 (N.D. Cal. 2007) ... 14

Skilling v. United States,
561 U.S. _____ (2010) ..... *passim*

United States v. Birnic,
193 Fed Appx. 528 (6th Cir.2003) 37

United States v. Daniel,
329 F.3d 480 (6th Cir. 2003) 36, 37

United States v. Grossman,
843 F.2d 78 (2d. Cir. 1988) 38

United States v.Males,
459 F. 3d 154 (2d Cir. 2006) 39

United States v. Marando,
504 F.2d 126(2d Cir. 1974) 38

United States v. Maze,
414 U.S. 395 (1974) 38

United States v. Mead,
533 U.S. 218 (2001) 23

United States v. Panarella,
277 F.3d 678 (3rd Cir. 2002) 44

Statutes

15 U.S.C. §80b-6 ..... *passim*

15 U.S.C. §80b-1 et seq. 15

18 U.S.C. § 1341 ..... 38, 39, 40, 42

Other Authorities

Investment Advisor Programs Under the Investment Company Act of 1940, 62 Fed.Reg. 15 (March 31, 1997) 17

Lowenstein, Roger (2000) "When Genius Failed: The Rise and Fall of Long-Term Capital Management" 31, 32

SEC FL. Release No. IA-2628; File No 57-25-06 25

S. Rep. No. 293, 104th Cong., 2d Sess. 10 (1996) 7

Staff Report to the United States Securities and Exchange Commission "Implication of the Growth of Hedge Funds (September 2003/"SEC Staff Report")" 3, 4

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MARK D. LAY,
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UNITED STATES OF AMERICA,
RESPONDENT.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

PETITION FOR A WRIT OF CERTIORARI

Mark D. Lay respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Sixth Circuit in this case.

OPINIONS BELOW

May 13, 2008 Opinion of United States district court, Northern District of Ohio entering judgment on a jury verdict against Mr. Lay.

July 11, 2008 Amended Judgment of United States district court, Northern District of Ohio.

July 14, 2010 Opinion of United States Court of Appeals for the Sixth Circuit affirming district court.

August 25, 2010 Order of United States Court of Appeals for the Sixth Circuit denying rehearing.

JURISDICTION

The judgment of the Sixth Circuit was entered on July 14, 2010. A Petition for the Rehearing and Rehearing En Banc was denied on August 25, 2010.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

STATUTES CITED TO IN PETITION:

15 U.S.C. §80b-6

15 U.S.C. §80b-1 et seq.

18 U.S.C. §1341

STATEMENT OF THE CASE

A. STATEMENT OF FACTS

This appeal arises from an unprecedented and stunning departure from established judicial precedent in relation to the regulation and prosecution of hedge fund investment advisers. The United States Security and Exchange Commission has defined a hedge fund as any pooled investment vehicle that is privately organized, administered by professional investment managers and not widely available to the public. *See*, Staff Report to the United States Securities and Exchange Commission

"Implications of the Growth of Hedge Funds (September 2003/"SEC Staff Report" at p. 3.").

This is an appeal from the conviction and sentence of Petitioner, Mark D. Lay, an African American, graduate of Columbia University, relating to his management of a hedge fund, in which the Ohio Bureau of Worker's Compensation (hereinafter referred to as "Bureau" or "OBWC") was an investor. Initially, on June 14, 2007, the government filed a four court indictment against Petitioner related to his involvement and/or his company's involvement with the Bureau and investments made by the Bureau into the MDL Active Duration Fund (hereinafter referred to as "ADF"), a hedge fund managed by Lay's company.

The following factual background details the specifics of the relationship between Petitioner and the Bureau. The Bureau or OBWC is an Ohio state agency that assists employers with expenses related to workplace injuries by providing medical and compensation benefits. The Ohio workers' compensation system is the largest exclusive state insurance fund in the United States, with assets of $14 billion and annual insurance premiums and assessments of $2.3 billion. OBWC exercises fiduciary authority with respect to the Ohio State

Insurance Fund (OSIF). This fund is held for the benefit of injured workers and employers of Ohio. OBWC invested funds into ADF on three discrete occasions, one hundred million dollars on August 20, 2003, one hundred million dollars on May 21, 2004 and twenty five million dollars on September 23, 2004. These are the only times OBWC "parted" with property at the behest of Petitioner, that is, it was on these three discrete occasions when funds left OBWC's custodial bank and were transferred to ADF. Other than these three occasions, OBWC did not part with money or property in connection with ADF by reason of any act of Petitioner.

Petitioner founded MDL Capital Management, Inc., (hereinafter referred to as "MDL") in 1992 and served as its Chairman, CEO, Principal Shareholder and Chief Investment Strategist. MDL was registered with the Securities and Exchange Commission (hereinafter referred to as the "SEC") as an investment adviser under the Investment Adviser's Act of 1940 hereinafter referred to as ("the Act").

In May of 1998 Petitioner and the OBWC entered into an Investment Management Agreement under which Petitioner would manage the OBWC's Long Fund, and also established MDL Capital, as an

investment adviser to OBWC under the Investment Advisers Act of 1940. OBWC allocated $355 million of its investment portfolio, referred to as the Long Fund, for management by MDL. There were no problems or questions about any conduct with regard to the Long Fund. It is not the Long Fund investment that is at issue in this appeal.

In May of 2002, Petitioner established ADF. ADF was established independently by Petitioner. OBWC did not finance or underwrite the expenses of establishing the ADF hedge fund. What is significant about ADF is that, unlike the Long Fund, as a portfolio managed by Petitioner for OBWC, ADF belongs to a class of investments that is exempt from the SEC regulatory framework applicable to the Long Fund and investments like it. In the case of the Long Fund, OBWC's funds remained in a custodial bank, Petitioner merely determined how to invest those funds. In the case of ADF, OBWC actually removed funds from its custodial bank and transferred them to ADF for investment by ADF. OBWC was merely an investor in ADF. OBWC had not right to control ADF investment strategy. Petitioner was the investment adviser to ADF. Petitioner was not an investment adviser to OBWC as it related to ADF. For this reason, theories of criminality or even civil

liability applicable to Petitioner's management of OBWC nonexempt investments are not necessarily pertinent to exempt investments such as ADF. In the case of ADF, Petitioner was not OBWC's investment adviser, as he was with the Long Fund. In connection with ADF Petitioner was ADF's adviser, OBWC was an investor only.

The regulatory framework respecting hedge funds acknowledges these truths and therefore reflects "Congress's view that certain highly sophisticated investors, [such as OBWC], do not need all of the protections of the Investment Company Act for the reason those Investors are in a position to appreciate the risks associated with pooled investment vehicles." *See*, S. Rep. No. 293, 104th Cong., 2d Sess. 10 (1996). "Generally, these investors can evaluate on their own behalf matters such as the level of a fund's management fees, governance provisions, transactions with affiliates, investment risks, leverage and redemption rights." *Id.* (Emphasis added). By entering into the hedge fund investment environment, OBWC accepted this risk. The decision by OBWC to invest in ADF was an overlay strategy.[2]

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2 ADF was part of an overall investment strategy being pursued by OBWC. It was part of what is called an "overlay strategy." An "overlay strategy" is an

The jury found that Petitioner, in violation of his fiduciary obligations under the 1940 Act, committed investment adviser fraud against OBWC by managing ADF in a manner inconsistent with leverage guidelines set forth within a private placement memorandum that outlined the terms and conditions of the ADF investments (hereinafter the "PPM"). Specifically, the government alleged that Mr. Lay exceeded guidelines set forth within the pertinent PPM by causing more than 150% of ADF's assets to be leveraged in connection with trades directed by Petitioner. The government alleged that mailing trade confirmation slips detailing these trades, although containing no false information, was mail fraud. As stated above, Petitioner was not an investment adviser for OBWC as to the ADF hedge fund. He was investment adviser to ADF. OBWC was merely an investor in ADF. According to the relevant PPM:

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investment strategy which is "overlaid" on top of existing strategies, and does not disturb existing investments. Overlay strategies can take many forms, such as currency overlays, interest rate overlays, cash management overlays, and many other types.

> The Fund is expected to leverage the Fund's investment portfolio as a means to increase yield and enhance total return. Up to 150% of the Fund's assets, at the time of investment, may be leveraged (*i.e.*, the combined value of borrowings and short positions). Leveraging will include, but is not limited to, short selling of securities, reverse repurchase agreements, certain option and futures transactions plus any borrowings to leverage the Fund's assets. Although the use of leverage may enhance returns on the Fund's portfolio and increase the number of investments that may be made by the Fund, it may also substantially increase the risk of loss. The percentage included above is intended as a guideline and may be changed from time to time at the sole discretion of the Board of Directors.

PPM at 3. (Emphasis added)

1. DURATION AND LEVERAGE

In the context of this appeal the issue of leverage is central. "Leverage means that the return on an owner's equity in a leveraged investment is not equal to the return on the investment, because the investment is not financed entirely with the owner's

money. For example, the owners fund may put up $1 billion of their own money, borrow $9 billion, and buy $10 billion in market value of Treasury bonds. The owners' equity (*i.e.*, the net asset value, or "NAV" of the fund) is $1 billion. One measure of leverage is the ratio of assets to equity, which is 10 in this example. Another measure of leverage is the debt-equity ratio, which is 9 in this example. If the bonds increase in value by 5%, or $0.5 billion, the NAV increases by the same amount (ignoring interest on the borrowing), and the return on equity is 50% (*i.e.*, $0.5 billion/$1 billion). The 50% increase in equity could be calculated by multiplying the asset-equity measure of leverage by the return on the bonds (*i.e.*, 10 x 5%).

Leverage, it is simple calculation that any sophisticated investor such as OBWC could calculate from the reports provided by Petitioner. It quite simply, is the overall position divided by the actual value of the position. Another example would be if a fund had a position of one billion dollars in bonds, but the portfolio had an actual value of 200 million dollars, the leverage would be 5 to 1 or 500%. Leverage will change based on changes to the overall position or changes in the value of the portfolio. Leverage is a calculation that changes from second to

second as the value of the portfolio changes with fluctuations in the market. Even if the actual position does not change, the leverage may change dramatically based on the market. If the value of the portfolio increases, the leverage will decrease and to the contrary if the value of the portfolio decreases, the portfolio leverage will increase. In the case of OBWC, the overlay strategy was to protect the portfolio against higher interest rates. The overlay strategy is a one way bet. It is not a strategy that capitalizes on various changes in the market. In this case, interest rates did not go higher but went lower. As rates went lower the value of the portfolio went down thus increasing the leverage substantially. All changes in leverage are therefore not simply attributable, as the government argued, to acts of Petitioner. Leverage may change simply by reason of market conditions. Here, the ADF portfolio continued to lose money as interest rates went lower. OBWC was aware of this and invested more cash in May 2004 which decreased leverage in ADF so ADF could operate. As ADF, an overlay strategy, lost money, the rest of the OBWC portfolio made money, thus you get the term "hedge". An overlay strategy is just a hedge for the rest of the portfolio. OBWC invested additional capital in ADF on two occasions,

after it was known that money had been lost. These investments are evidence of OBWC's sophistication and their ability to determine the value of the ADF portfolio.

Despite the above, the jury found that Mr. Lay violated Section 80b-6 of the Act, by repeatedly exceeding the above leverage guideline. The superseding Indictment stated by reason of Mr. Lay's fraud and deceit upon the OBWC by using leverage in excess of 150% and not informing OBWC or gaining its consent, OBWC lost $216,000.000 of its $225,000,000 ADF investment. Counts 2, 3 and 4 of which Petitioner was also convicted alleged conspiracy, wire and mail fraud, and aiding and abetting offenses based upon Petitioner's alleged misrepresentations and nondisclosures relating to how much leverage had been utilized in connection with ADF trading. These convictions must be reversed as a matter of law for the reason Petitioner was not OBWC's investment adviser in relation to ADF, OBWC was a sophisticated investor, and there was no use of the mail of wires to cause OBWC to part with money.

B. COURSE OF PROCEEDINGS

The trial for this matter began on October 12, 2007, with the selection of a jury. The trial itself began on October 15, 2007. The trial concluded with guilty verdicts returned by the jury on October 30, 2007, to investment advisory fraud, mail and wire fraud, conspiracy to commit or attempt mail and wire fraud, and aiding abetting. In addition, the jury returned a verdict regarding the issue of forfeiture, finding that the proceeds that were obtained and subject to forfeiture constituted the sum of $590,526.23 and $212,967,084.76 in restitution.

Following the conviction, Petitioner was released on bond pending sentencing. Petitioner filed a Motion for Acquittal, or in the alternative, a Motion for a New Trial, on November 13. 2007. After the government's response and oral argument on May 5, 2008, the District Court entered a Memorandum Opinion and Order on May 13, 2008, (R.158) denying Lay's motions.

A sentencing hearing was held on July 3, 2008 and July 8, 2008. A judgment was thereafter entered and on July 9, 2008, Lay was sentenced to 60 months as to Count 1 and 144 months as to each of counts 2, 3 and 4.

Petitioner appealed the decision of the District Court. Timely appeal was filed in the Sixth Circuit.

REASON FOR GRANTING THE PETITION

THE SIXTH CIRCUITS FAILURE TO FOLLOW GOLDSTEIN HAS CREATED A CONFLICT BETWEEN THE COURTS

a. Investment Adviser's Act and Goldstein

Federal law determines whether a fiduciary relationship exists in relationships governed by the Investment Advisor's Act. Specifically, Section 206 of that Act governs whether a fiduciary duty is owed from an investment adviser, or adviser to a ADF Hedge Fund, to their 'client.' *Goldstein v. SEC*, 451 F. 3d 873, 881 (D.C. Cir. 2006); see also *SEC v. Trabluse*, 526 F. Supp.2d 1008 (N.D. Cal. 2007)(stating that with respect to the Investment Adviser's Act of 1940, the Securities and Exchange Commission must show a breach of fiduciary duty to the fund itself since the adviser owes a duty only to the fund and not the fund's investors). Also see, *SEC v. North Shore Asset Management*, 2008 U.S. Dist. LEXIS 36160 (S.D. NY May 5, 2008) (SEC can not bring actions against hedge fund advisers where

investments are defrauded). Specifically, "*U.S.C.S. §. 80b-1 et seq.*, makes it unlawful for any investment adviser, registered or not, to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client." *Goldstein*, 451 F.3d at 881. Additionally, "The United States Supreme Court has held that 12 U.S.C.S. § 80b-6(2) created a fiduciary duty of loyalty between an adviser and his client which required the adviser to disclose self interested transactions to him." *See SEC v. Capital Gains Research Bureau*, 375 U.S. 180, 191-92 (1963).

An accurate understanding of the *Goldstein* case is pivotal to this appeal. Therein, the D.C. Circuit court stated that it was "counterintuitive" to characterize the investors in a ADF Hedge Fund as the "clients" of the adviser. *Goldstein*, 451 F.3d at 881. The adviser owes a fiduciary duty only to the fund itself, not to the fund's investors. *Goldstein* further states that Congress did not intend "shareholders, limited partners, or beneficiaries" of a ADF Hedge Fund to be counted as "clients." Id. At 879. Here there was no investment adviser's agreement between Petitioner and OBWC as to ADF. There was a specific exclusive investment adviser's

agreement between ADF and Petitioner of which OBWC was aware.

The fund manager -- the adviser -- controls the disposition of the pool of capital in the fund. The adviser does not tell the investor how to spend his money; the investor made that decision when he invested in the fund. *Id.* at 880. Having bought into the fund, the investor fades into the background. *Id.* His role has become completely passive. *Id.* If the person or entity controlling the fund is not an "investment adviser" to each individual investor, then a *fortiori* each investor cannot be a "client" of that person or entity. *Id.* In *Goldstein*, the court states that the "kind of fiduciary relationship the Act was designed to regulate is the "type of direct relationship [that] exists between the adviser and the fund, but not between the adviser and the investors in the fund." *Id.*

The Courts below correctly analyzed and cited to Goldstein, and recognized that *Goldstein* concluded that "hedge fund investors are not clients of the fund adviser . . ." The Courts also quoted *Goldstein's* analysis pertaining to the structure of hedge fund relationships. Prior to the SEC's new rule attempting to expand the definition of hedge fund client, the SEC explained that:

> "a 'client of an investment adviser typically is provided with individualized advice that is based on the client's financial situation and investment objectives. In contrast, the investment adviser of an investment company need not consider the individual needs of the company's shareholders when making investment decisions, and thus has no obligation to ensure that each security purchased for the company's portfolio is an appropriate investment for each shareholder.'"

(MOO, Doc, #158, p. 28-9)(quoting *Goldstein*, 451 F.3d at 880, quoting Status of Investment Advisor Programs Under the Investment Company Act of 1940, 62 Fed. Reg. 15, (March 31, 1997)).

The Courts below further correctly quoted *Goldstein's* holding that "hedge fund investors are not client's of the fund's investment adviser" because conflicts of interest would be "inevitable" if the adviser owed a fiduciary duty to "act in the client's best interest, and fully disclose material conflicts the adviser has with his clients, to both the fund and the fund's investors." *Id.* (citing *Goldstein*, 451 F.3d at 881).

The Sixth Circuit correctly observed that the Goldstein court struck down the SEC rule defining ADF Hedge Fund investors as clients because to do so would manipulate the meaning in that "The Commission has, in short, not adequately explained how the relationship between ADF Hedge Fund investors and advisers justifies treating the former as clients of the latter." *Id.* (citing *Goldstein*, 451 F.3d at 882).

Moreover, and truly applicable to the present appeal, the trial Court recognized that the *Goldstein* court did not accept the SEC's argument that different classes of investors should be treated differently because if there are "certain characteristics present in certain investor-advisor relationships that mark a "client" relationship, then the Commission should have identified those characteristics and tailored its rule accordingly." *Id.* (citing *Goldstein*, 451 F.3d at 882-83).

To state it more succinctly, the Circuit Court itself accepted the *Goldstein* ruling that an investor in a hedge fund is not a client of the adviser to the fund. Moreover, the Circuit specifically stated that the lack of a fiduciary relationship between the advisor to the fund and the investors in the fund is not altered by the facts of a particular case, i.e. as a

matter of law, the investors in the fund are not clients of the fund's advisor and no fiduciary duty is owed.

What follows in the District Court's opinion is perplexing, to say the least. Directly contrary to its immediately preceding legal analysis, the District Court stated that "the facts of *Goldstein* . . . are very different than the facts of this case." And went on to find that, based upon the facts of this case, there was a fiduciary duty owed. The District Court held in direct opposition to the case law it cited to support its position. The Sixth Circuit affirmed this erroneous conclusion.

As admitted by the government and the District Court the primary governing document that established the parameters of the business relationship between Mark Lay, the ADF Hedge Fund and the Bureau, is the PPM dated January 15, 2003. In that document, it is abundantly clear that the client was the ADF Hedge Fund, that the Bureau was an investor in the fund and that "the director's principal duty is to act in the best interest of the Company[,]" i. e., the ADF Hedge Fund. (PPM p. 23). Undeniably, Mark Lay's fiduciary responsibilities here were to the ADF Hedge Fund, not OBWC.

As investors, the Bureau was repeatedly advised and encouraged to seek outside counsel to evaluate their involvement with the ADF Hedge Fund. The Bureau was told that they could not reply upon the advice of Mark Lay and MDL, the advisor to the ADF Hedge Fund: "The investors [are] not represented by [the experts to the ADF Hedge Fund.] Each prospective investor should consult his own legal, tax and financial advisers regarding . . . the suitability of an investment in the [Hedge] Fund." (PPM p. 23). The Bureau is never referred to as a client in the PPM. Moreover, it is obvious from a comprehensive reading of the PPM that one of its primary purposes is to establish the arms length relationship between *investors* in the ADF Hedge Fund and the advisers to the ADF Hedge Fund.

It is beyond dispute that the Sixth Circuit erred in failing to find that, as a matter of law, the Bureau was not the client of MDL as the adviser to the ADF Hedge Fund. *Goldstein* makes is clear that due to the reality of the ADF Hedge Fund investment vehicle and the manner in which it must be administered, it is counterintuitive that the Bureau was a client.

b. Fiduciary Relationship

A fiduciary relationship can only be created when both parties understand that a special trust or confidence has been reposed. *Aschinger v. Columbus Showcase Co.*, 934 F.2d 1402, 1408 (6th Cir. 1991). Such a relationship cannot be predicated on one party's allegedly superior knowledge of the facts of a particular transaction when the relevant facts are readily available to both parties. *Id.* at 1408.

The PPM repeated, over and over again, that the investors were to seek outside counsel and advice from its own financial advisor before even entering into the agreement as well as when deciding if and how much to invest in the ADF Hedge Fund.

Moreover, the PPM virtually screams to potential investors that the ADF Hedge Fund is an extremely risky investment. Potential investors are warned, cautioned and advised of all material facts that may affect their investment, including the risk that their total investment may be lost. Potential investors are warned cautioned and advised to seek outside consultation before choosing to invest. The PPM states:

> There is a high degree of risk associated with an investment in the Fund and an investment in the Fund should only be

> made after consultation with independent qualified sources of investment and tax advice.

(PPM, p. 17).

As to risks, the PPM states again, also in all capital letters:

> THE SHARES ARE SPECULATIVE AND INVOLVE A HIGH DEGREE OF RISK. THEY ARE SUITABLE ONLY FOR PERSONS WHO CAN AFFORD TO LOSE THEIR ENTIRE INVESTMENT. SHAREHOLDERS SHOULD READ THE MEMORANDUM AND ARTICLES OF ASSOCIATION AS WELL AS THE FUND'S CONTRACTS WITH SERVICE PROVIDERS WHICH ARE REFERENCED IN "STATUTORY AND GENERAL INFORMATION."

(PPM, p. 24)(emphasis in original).

On September 10, 2008, the SEC amended its rules for enforcement actions under §80b-6, the statute under which Mr. Lay was prosecuted, in response to the opinion in *Goldstein v. SEC*, 451 F. 3d 873 (D.C. Cir. 2006). While *Goldstein* is not

binding authority in the Sixth Circuit, the interpretation of the SEC concerning the operation of §80b-6 is entitled to great deference from a federal court. *United States v. Mead*, 533 U.S. 218 (2001) and *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). The Sixth Circuit attempted to distinguish *Goldstein* by stating it does not stand for the proposition that an investor may never be the client. This is exactly what Goldstein says is never possible. In point of fact, *Goldstein* states:

> An investor in a private fund may benefit from the adviser's advice (or he may suffer from it) but he does not receive the advice *directly*. He invests a portion of his assets in the fund. The fund manager-the advisor-controls the disposition of the pool of capital in the fund. The adviser does not tell the investor how to spend his money; the investor made that decision when he invested in the fund. Having bought into the fund, the investor fades into the background; his role is completely passive. If the person or entity controlling the fund is not an "investment adviser" to each individual investor, then a *fortiori* each investor cannot be a "client" of that person or

entity. These are just two sides of the same coin.

* * *

If the investors are owed a fiduciary duty and the entity is also owed a fiduciary duty, then the adviser will inevitably face conflicts of interest. Consider an investment adviser to a hedge fund that is bankrupt. His advice to the fund will likely include any and all measures to remain solvent. His advice to an investor in the fund, however, would likely be to sell. For the same reason, we do not ordinarily deem the shareholders in a corporation the "clients" of the corporation's lawyers or accountants. *see* RESTATEMENT, *supra*, §96 cmt. b ("By representing the organization, a lawyer does not thereby also form a client-lawyer relationship with all or any individuals. . . who have an ownership or other beneficial interest in it, suck as its shareholders."). While the shareholders may benefit from the professionals' counsel indirectly, their individual interests easily can be drawn into conflict with the interest of the entity. It simply cannot be the case that investment advisers are the servants of two masters in this way.

Goldstein, pp. 11-12, 15. (Emphasis in the original and emphasis added)

Under the *Chevron* doctrine it was determined that a federal court should defer to an agency's interpretation of a statute if the agency's interpretation is reasonable or permissible and the statute is ambiguous or there is a gap that Congress intended the agency to fill.

When the *Chevron* rule is applied here, you have the SEC revisiting its rules concerning the reach of §80b-6 in response to an opinion, *Goldstein*, that states unequivocally - hedge fund investors can never be clients of the investment advisor, and point two - a point the United States has failed to address, investment advisors owe no fiduciary duties to hedge fund investors. In point of fact, SEC FL. Release No. IA-2628; File No 57-25-06 states in p. 13: "206(4)-8 does not create under the Advisors Act a fiduciary duty to investors or prospective investors in a pooled investment vehicle not otherwise imposed by law." *Goldstein* stated unequivocally, prior to passage of this new rule, that advisors did not owe investors any fiduciary duties. As such there were no other fiduciary duties imposed by law.

Here, the prosecution under §80b(6)(1) and (2) depended on a requirement to find the OBWC was

Petitioner's client, in relation not the ADF, a status that was determined as a matter of law in *Goldstein* not to exist. The prosecution under §80b-6(4), the catchall, depended on a requirement that the jury find that Petitioner was an investment adviser to OBWC and owed fiduciary duties to the OBWC in relation to the ADF, duties which *Goldstein* stated that advisors do not owe. The SEC rule was amended to clarify that a new provision Rule 206(4)-8 would delineate that conduct required under §80b-6 as it relates to investors or prospective investors. Section 80b-6 in its entirety is only applicable to investment advisers in relation not the relevant investment here, ADF, Petitioner was not OBWC's adviser, so 80b-6 has no applicability at all.

ADF had a separate and distinct relationship with Petitioner. There is some question whether OBWC was even authorized to invest into ADF or any other hedge fund. The OBWC policy authorizing alternative investments was not approved until 2004, after the initial investments here.

ADF was intended to receive the investment of the OBWC and potentially other investors as well. The fact the OBWC ended up as the sole investor in ADF, does not change OBWC's status as merely an investor.

It was common knowledge now and at the time this fund was created that a hedge fund is a high risk investment vehicle. That is why it is limited to sophisticated investors. Concomitant with the potential for high gains is the risk of substantial losses, including the total loss of the investment. (PPM p. 24). It is for this reason that a different set of rules and regulations apply to hedge funds. These rules and risks were fully described and outlined in the PPM, the documentation that governed the subject of ADF Hedge Fund and that delineated the terms of the agreement between the OBWC, the ADF Hedge Fund, MDL and Mark Lay. By entering into the agreement, OBWC accepted these terms and these risks. Pursuant to the agreement, OBWC chose to accept the lack of fiduciary relationship and the risks and potential for a total loss of its investment due to unforeseen volatility of the market.

1. ADF Hedge Fund Established as the Client of MDL and OBWC Established as an investor in the ADF Hedge Fund: Fiduciary Duty Owed to the ADF Hedge Fund as a Whole and Did Not Extend to Individual Investors.

OBWC specifically, unambiguously and unequivocally accepted that the ADF Hedge Fund was the client of MDL. OBWC accepted that it was an *investor* only in the ADF Hedge Fund, and that it was not a *client* of Mark Lay with respect to the ADF Hedge Fund. (PPM, p. 18). An investor in an ADF Hedge Fund is not the same thing as a client of the ADF Hedge Fund. Mark Lay's obligation with respect to the ADF Hedge Fund was to make investments that profited the fund, not the individual investors in the ADF Hedge Fund. (PPM, p. 18)

That OBWC is an investor in the ADF Hedge Fund and not a client is reiterated throughout the PPM. Any investor in the ADF Hedge Fund, including the OBWC, was advised to seek outside advice and counsel before entering into the agreement. Potential investors were specifically told not to rely upon the investment adviser to the ADF Hedge Fund, MDL, nor the ADF Hedge Fund's or Investment Adviser's experts, but were to seek their own investment advice and their own independent expert advice. The Sixth Circuit Opinion creates a relationship that was expressly negated by the relevant transaction documents.

Several specific examples of this exist in the PPM. At the outset of the PPM, it is stated, in all capital letters:

> PROSPECTIVE SUBSCRIBERS IN THE FUND SHOULD INFORM THEMSELVES AS TO THE LEGAL REQUIREMENTS AND TAX CONSEQUENCES WITHIN THE COUNTRIES OF THEIR RESIDENCE AND DOMICILE FOR THE ACQUISITION, HOLDING OR DISPOSAL OF SHARES AND ANY FOREIGN EXCHANGE REGISTRATIONS WHICH MAY BE RELEVANT TO THEM. IF YOU ARE IN ANY DOUBT ABOUT THE CONTENTS OF THIS MEMORANDUM, YOU SHOULD CONSULT YOUR STOCKBROKER, SOLICITOR, ACCOUNTANT OR OTHER FINANCIAL ADVISER.

(PPM, p. ii).

In the body of the PPM, it is stated:

> *Lack of Independent Experts Representing Investors.* The Fund and the Investment Adviser have each

> consulted with counsel, accountants and other experts regarding the formation and terms of the Fund and the Advisory Agreement. The investors, however, have not been represented by such independent experts. Each prospective investor should consult his own legal, tax and financial advisers regarding the desirability of purchasing shares and the suitability of an investment in the Fund. Foley and Lardner and Appelby, Spurling & Kempe are a U.S. and Bermuda counsel to the Fund, respectively, and do not represent the prospective investors or shareholders of the Fund.

(PPM, p. 23). (emphasis in the original).

Also stated clearly and unambiguously was that the ADF Hedge Fund would be managed by a Board of Directors, which would have absolute discretion as to when and how to invest. The Board consisted of Mark. D. Lay, Steven L. Sanders, and Edward Adatepe, who were the principals of MDL and Oskar P. Lewnowski and Raymond Morrison of Olympia Capital International Inc., which was the Fund's administrator (PPM, p. 18). The PPM further states that the investments made on behalf of the

ADF Hedge Fund would be determined by the Board and that "The Investment Adviser, in its sole and absolute discretion and authority as an investment adviser to the fund will ultimately identify and select investments for the Fund." (PPM, p. iv). (Emphasis in the original).

2. Percentage of Assets Permitted to be Leveraged Within Sole Discretion of Hedge Fund Board of Directors.

A highly critical fact to appreciate for this appeal is the percentage of assets the OBWC agreed that the ADF Hedge Fund Board and Mark Lay could leverage. The PPM, the primary governing document for the agreement between the OBWC and MDL, states that the leverage *guideline* is up to 150% of the Fund's assets at the time of investment. (PPM, p. 3). This figure is a *guideline*. It is not a limitation and it is not a prohibition, it is a "guideline".[3]

---

[3]Note in the case of Long Term Capital Management, a 100 billion dollar hedge fund established in 1994 by John Meriwether Vice Chair, now a head of bond trading at Saloman Brothers, at the time of the 1998 collapse the funds assets had been over leveraged 250-1. LTCM's collapse threatened the stability of the entire American market. There were no criminal prosecutions. See,

It is indisputable that the PPM grants the Board of Directors absolute and sole discretion to exceed the guideline when it determines that it is in the best interest of the ADF Hedge Fund to do so. This fact is acknowledged by Terry Gasper, the Chief Financial Officer of the OBWC. Terry Gasper testified that he understood the PPM to give the Board of Directors the sole discretion to change the guideline, and that they could do so at any time, without notice. (Testimony T.C. Gasper, Doc. #102, pp. 134-135). In addition, the PPM, which was signed by the officers of the OBWC, states:

> **The percentage included above is intended as a guideline as may be changed from time to time at the sole discretion of the Board of Directors.**

(PPM, p. 3). (emphasis added)

The grant of authority to Mark Lay, as to the ADF Hedge Fund, could not be clearer.

3. Risk Factors and all Relevant Facts Explained and Agreed Upon By OBWC

Lowenstein, Roger (2000) "When Genius Failed: The Rise and Fall of Long-Term Capital Management"", Random House.

In the PPM, MDL went to great lengths to explain the risk factors of the ADF Hedge Fund in unambiguous terms. For example, at the very beginning of the PPM it is stated in bold capital letters:

> **THE PURCHASE OF SHARES IS SPECULATIVE AND INVOLVES A HIGH DEGREE OF RISK, THERE IS NO ASSURANCE THAT THE FUND WILL BE PROFITABLE. SEE THE SECTION ENTITLED "RISK FACTORS" WITHIN THIS MEMORANDUM FOR A DESCRIPTION OF CERTAIN RISKS INVOLVED IN THE PURCHASE OF SHARES.**

(PPM, p. iii) (Emphasis in the original).

Specifically as to the risks of leverage, the PPM states that is the 150% guideline is not enough to cover a decline in value, additional collateral may be required:

> Risks of Leverage. If the Fund's assets decline in value or there are significant redemptions from the Fund, the Fund may be required to post additional

> collateral with the lender or liquidate assets to pay off its borrowings. Moreover, if the assets under management are not sufficient to pay the principal of and interest on the debt when due, the Fund could sustain a total loss of its investment.

(PPM, p. 19).

It is important to reiterate here that the PPM was ambiguous that:

> **The percentage included above is intended as a guideline and may be changed from time to time at the sole discretion of the Board of Directors.**

(PPM, p. 3). (Emphasis added.)

The PPM further makes clear to those who chose to invest in the ADF hedge Fund that there is a potential for conflicts of interests to arise between the fund and other clients of MDL. (PPM, p. 16). By agreeing to the terms of the PPM, the investors in the ADF Hedge Fund accepted the potential that the investment adviser may engage in transactions or investments for its own account or the account of any other client, that may not benefit the ADF Hedge

Fund, but if they do so invest, it shall be in good faith and on a fair and equitable basis. (PPM, p. 17).

The OBWC anticipated, as did many others, that if long term interest rates had increased in 2003-2004, the ADF Hedge Fund would have been highly successful. However, long term interest rates did not rise and losses were sustained due to the unexpected events in the markets. There was absolutely no gain to Mr. Lay.

In *Goldstein*, the Court discussed at length the distinction between an investor and a client in the context of hedge funds. "At best it is counterintuitive to characterize the investors in a hedge fund as the client of the adviser's. *Id* at 883. Citing *Am. Bar Ass'n v. FTC*, 368 U.S. App. D.C. 368, 430 F.3d 457 (D.C. Cir. 2005). (Emphasis added.)

The Sixth Circuit Opinion does exactly what *Goldstein* points out as counterintuitive, states contrary to *Goldstein's* prohibition, that an investment advisor may indeed serve two masters, the investor and the client.

c. Wire Fraud and Mail Fraud

The evidence did not establish that Mr. Lay was guilty of either mail or wire fraud, aiding and abetting, or a conspiracy to commit either. This

assertion is true as a matter or law, for the reason there was no evidence at all that money or property was obtained through a material misrepresentation or that the mail or wires were used in furtherance of a scheme to obtain money or property. OBWC parted with property voluntarily on three occasions, when it invested in ADF, not when the trades directed by Petitioner occurred. This is a fatal defect in this prosecution.

The Sixth Circuit has stated: "mail fraud cases may be used to analyze wire fraud cases." *United States v. Daniel*, 329 F.3d 480, 487 (6th Cir. 2003).

> The Supreme Court construed the statute to "include[e] everything designed to defraud by representations as to the [*15] past or present, or suggestions and promises as to the future." *Neder*, 527 U.S. at 24 (quoting *Durland, 161 U.S. at 313*). Accordingly, the Court held that materiality of falsehood is an element of the federal mail fraud, wire fraud, and bank fraud statutes. *Neder, 527, U.S. at 25.*
>
> In general, a false statement "is material if it has 'a natural tendency to

> influence, or [is] capable of influencing, the decision of the decision-making body to which it was addressed.'" *Id. at 16* (*quoting United States v. Gauding, 515 U.S. 506, 509, 115 S. Ct. 2310, 132 L.Ed. 2d 444 (1995)*). The misrepresentation or omission must have th purpose of inducing the victim of the fraud to part with property or undertake some action that he would not otherwise do absent the misrepresentation or omission. *United States v. Daniel*, 329 F. 3d 480, 487 (6th Cir. 2003).

United States v. Birnic, 193 Fed Appx. 528, 534, (6th Cir.2003).

First with respect to materiality, "It is clear that as an element of the "scheme or artifice to defraud "requirement, the government must prove that the defendant said something materially false." *Daniel* at 486. There was no evidence of Mr. Lay uttering a false statement related to ADF that caused OBWC to part with money and sending it by wire or mail.

Here the government alluded on pp. 13-16 in the Superseding Indictment to trade confirmation statements. These confirmation statements do not contain false information. What's more, in cases

where mailing trade confirmation statements constituted a violation of 18 U.S.C. §1341, the statements were transmitted for the purposes of executing the artifice or scheme. *See, United States v. Marando*, 504 F.2d 126(2d Cir. 1974) where trade confirmation slips were mailed and determined to be an integral part of a scheme to *obtain* property; *also see, United States v. Grossman*, 843 F.2d 78 (2d. Cir. 1988) where it was determined that:

> The mailings of the confirmation slips did further the purpose of executing the scheme. The confirmation slips (1) notified the relatives that the purchase or sale actually had been completed; (2) provided an on-going tally of purchases, allowing the relatives to cover each other's positions; (3) concealed the fraud by maintaining an appearance of normality, *see United States v. Cohen, 518 F.2d 727, 737 (2 Cir.), cert. denied, 423 U.S. 926, 46 L. Ed. 2d 252 (1975)*; and (4) allowed the relatives to demonstrate ownership after the recapitalization announcement. *Pereira v. United States, 346 U.S. 1, 98 L. Ed. 435, 74 S. Ct. 358 (1954)*. [**27]

To establish a violation of the mail fraud statute, "the mailing must be for the purposes of executing the scheme." *United States v. Maze*, 414

U.S. 395 (1974). To state an offense under 18 U.S.C. §1341 the Supreme Court determined in *Cleveland v. United States*, 531 U.S. 12 (2000) that the Indictment must allege that the defendant not only devised a scheme or artifice, but also used that scheme or artifice to obtain money or property. *See, United States v.Males*, 459 F. 3d 154 (2d Cir. 2006) (Emphasis added). Here the Indictment states ADF received its first $100,000,000.00 before Mr. Lay ever executed a trade. At best the allegations here establish that having lawfully obtained property, Mr. Lay abused the property by investing it in a manner inconsistent with PPM guidelines. The mail was not used to obtain money or property here. There are no facts alleged that indicate that property or money was obtained through a scheme that involved a use of the mail. The trade confirmation slips here unlike in Grossman or Mirando did not contain false information, did not document illegal insider trades, and were not transmitted to obtain money or property. The alleged nondisclosures and misrepresentations concerning leverage alleged in the Indictment are not related to the mailing of confirmation slips. The trades reflected on the listed slips were lawful trades for a hedge fund. It does not matter that OBWC did not authorize them, the PPM

gave ADF's board sole discretion to deviate from the leverage guideline not OBWC. The trade confirmation statements report the purchases of bonds on a certain date, from a certain broker, at a certain price. All of this information is true. On these facts a violation of 18 U.S.C. §1341 was not established.

If the jury believed that the scheme or artifice to defraud was the initiation of trades by Mr. Lay utilizing excess leverage, employing excess leverage is not a misrepresentation for the purpose of inducing a victim to part with property. The facts here establish OBWC invested funds in ADF on three discrete dates, August 20, 2003, May 21, 2004 and September 23, 2004. These are the only times OBWC "parted" with property. The Indictment does not focus on these events. This is contrary to well established Sixth Circuit authority. In point of fact:

> "Mail fraud consists of (1) a scheme or artifice to defraud; (2) use of mails in furtherance of the scheme; and (3) intent to deprive the victim of money or property." *United States v. Turner, 465 F.3d 667, 680 (6th Cir. 2006).* Materiality of falsehood is a requisite element of mail fraud. Neder *v. United States, 527 U.S. 1, 25, 119 S. Ct. 1827,*

> *144 L. Ed. 2d 35 (1999)* The misrepresentation "must have the purpose of inducing [*7} the victim of the fraud to part with the property or undertake some action that he would not otherwise do absent the misrepresentation or omission." *United States v. Daniel, 329, F.3d 480, 487 (6th Cir. 2003).* A misrepresentation "is material if it has a natural tendency to influence, or is capable of influencing, the decision of the decision-making body to which it was addressed." *Neder*, 527 U.S. at 16 (internal citation and quotation marks omitted).

McCauliff, supra.

There was no evidence here that the OBWC parted with property by reason of a material misrepresentation.

> The mail fraud stated "does not purport to reach all frauds, but only those limited instances in which the use of the mails is part of the execution of the fraud." *Kann v. United States*, 323 U.S. 88, 95, 89 L.Ed. 88, 65 S. Ct. 148 (1944). Accordingly, the government must show beyond a reasonable doubt that [defendant] caused the mailings listed

> in the indictment to be sent and that the mailings were in furtherance of the fraud.

United States v. Pimental, 236 F. Supp. 2d 99 (D.C. Mass 2002).

Here there was no proof of any mailings in further of a scheme to exceed leverage or that the OBWC parted with money due to a mailing. The same deficit applies to Counts 3 and 4.

d. The Sixth Circuit Failed To Follow Skilling

Aside from the above, on June 24, 2010, the United States Supreme Court in *Skilling v. United States*, 561 U.S. _____ (2010), No. 08-1394, announced a seismic shift in mail fraud prosecutions. The Sixth Circuit totally ignored the *Skilling* opinion.

The *Skilling* opinion highlights what the government's burden of proof is in a prosecution under 28 U.S.C. § 1341 for mail fraud, one of the offenses that Mr. Lay is charged with here. *Skilling* makes it clear that an essential element in a mail fraud prosecution is evidence of some form of gain or enrichment to the defendant. In point of fact, *Skilling* states:

> Enacted in 1872, the original mail-fraud provision, the predecessor of the

> modern-day mail- and wire-fraud laws, proscribed, without further elaboration, use of the mails to advance 'any scheme or artifice to defraud.' *See, McNally v. United States*, 483 U. S. 350, 356 (1987). In 1909, Congress amended the statute to prohibit, as it does today, 'any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises.' §1341 (emphasis added); see id., at 357-358. Emphasizing Congress' disjunctive phrasing, the Courts of Appeals, one after the other, interpreted the term "scheme or artifice to defraud" to include deprivations not only of money or property, but also of intangible rights.

Id. (emphasis added) *Skilling* goes on to discuss the elements of a honest services fraud claim versus other frauds. The Court focuses on the requirement for symmetry, in a standard mail fraud case, that is "the victim's loss of money or property supplied the defendant's gain, with one the mirror image of the other.' *Id.*

In this case it is undisputed that Petitioner did not realize any gain as a result of an alleged misuse of the mails. The victim, the Ohio Bureau of Workers

Compensation (OBWC), losses were due to unsuccessful attempts by Petitioner to recoup losses through increased use of leverage. In some instances gains resulted from the use of increased leverage. In other instances losses occurred from its use. In no instance, however, did Petitioner realize any money or property from the use of allegedly excessive leverage. In most instances leverage changed due to market fluctuations, not Petitioner's acts.

Petitioner received no compensation from OBWC by reason of trading activity or volume. All of Petitioner's fees were paid by the Active Duration Fund (ADF), not the OBWC. Mr. Lay received no compensation from OBWC for ADF trades or managing OBWC funds.

The absence of any gain of any nature by a defendant is fatal to a mail fraud prosecution. *Skilling* emphasizes this point.

The use of excessive leverage was not a scheme to defraud. It was an investment strategy that failed. The purpose and intent of the strategy was not of a nature that will support a mail fraud prosecution. *See, Skilling (citing, United States v. Bloom*, 149 F. 3d. 649, 655 (7th Cir. 1998) and *United States v. Panarella*, 277 F.3d 678, 692 (3rd Cir. 2002) (requires that a defendant act in pursuit of private gain)).

Skilling determined that a 28 U.S.C. § 1346 prosecution requires as "offense conduct" evidence of either bribery or kickbacks and that the ambit of a criminal statute should be resolved in favor of lenity. *Rewis v. United States*, 401 U.S. 808 (1971). The "offense conduct" in Petitioner's case, a 28 U.S.C. § 1341 prosecution, according to *Skilling*, the conduct must include an element of gain at the expense of a victim, here OBWC.

In this case the gain element is totally lacking. In point of fact, the District Court states at p. 23 of Petitioner's sentencing memorandum. Case no. 1:07 CR-00339- DOD:

> As the Court undertakes a study as to the seriousness of the offense and the need to impose the sentence that promotes respect for the law and provides just punishment for the defendant's conduct, the defendant's sentencing memorandum reviewing the defendant's past history including his past business, is relevant. The defendant recites the fact that he opened his business known as MDL Capital in 1994 beginning only with a telephone and receptionist and built the business into a highly successful venture, employing over 40 people. His

counsel contends that he 'became one of the nations better recognized financial commentators, appearing regularly on MSNBC and on business related shows. His opinions were reflected frequently in the Wall Street Journal. He was selected as the Entrepreneur of the Year in Pittsburg by the accounting firm of Ernst & Young.' Continuing, his counsel recite the fact that the Long Fund (or the Core Fund) made money as did the state of Ohio generally. His counsel contend 'the fact is that the circumstances of the market developed in a way never before experienced. Looking back in hindsight, as the Court can do, *it seems obvious that he should have stopped following the investment strategy he had in place. But at the time, no one had ever seen an instance in which rising bond prices would not lead to a devaluation of existing bonds.* But that is precisely what happened in this time frame. *It was the first time in economic history of the United States that that occurred*, and his strategy failed, and because of the leverage, failed dramatically.'

* * *

It seems apparent that the defendant had not lost any monies for any clients

> in the management of the MDL investments until the defendant began excessive over-leveraging with the ADF. It appears from his past experiences with Mellon Bank and PNC that it was not the first time defendant took great risks in the belief that he could recoup his losses. The Court notes that the defendant, born in 1963, actively pursued a good education and did not demonstrate criminal tendencies. The defendant has no criminal record. The defendant appears to have been a responsible father. *It does not appear to the Court that the defendant was motivated to gain more income by his management of the ADF.*

Id. (emphasis added)

As the District Judge indicated, there was no evidence whatsoever that the mails were used by Petitioner in any scheme to defraud another or to generate gain for Mr. Lay. *Skilling* makes it clear the absence of this element is fatal to a mail fraud prosecution. The mailing of trade confirmation slips by third parties that document specific transactions, did not result in any gain or benefit to Mr. Lay.

Aside from the clarification provided by *Skilling* in relation to mail fraud prosecutions, Skilling also explains that Constitutional error occurs

where a jury is instructed on alternative theories of guilt and returns a general verdict that may rest on a legally invalid theory.

In this case, the jury was instructed in connection with each of the four counts on alternative theories of liability. In each instance here, the jury was permitted to find that Petitioner was an investment adviser without any requirement to also determine whether he was an investment adviser to the alleged victim, or whether the victim was an investor as distinguished from Mr. Lay's client. The jury was also permitted to determine that the OBWC was Petitioner's client, a determination which *Goldstein v. SEC*, 451 F.3d 873 (D.C. Cir. 2006) states, is a determination for the Court, not for the jury.

e. Limiting Instructions

Following the reading Petitioner's civil deposition testimony to the jury, the district court refused to give the proper limiting instruction specifically required in *United States v. Marvin Smith* 419 F. 3d 521 (6th Cir. 2005) that cautioned the jury not to place too much emphasis on the testimony or take it out of context. The district court only advised the jury not place too much emphasis on the testimony. The Sixth Circuit specifically requires a

two pronged caution, not the single prong given by the Court. The prejudice to Petitioner is palpable for the reason this instruction concerns the client-investor dichotomy. The district court's failure to give the two pronged instructions permitted the jury to take Petitioner's testimony out of context.

CONCLUSION

For the above reasons, the Court of Appeals should be reversed and Petitioner's conviction vacated.

November 23, 2010

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APPENDIX

SIXTH CIRCUIT COURT APPEALS FILINGS:

Order Denying Petition
for Rehearing,
filed 08/25/10 ..... A1 - A2

Opinion,
filed 07/14/10 ..... B1 - A27

NORTHERN DISTRICT OF OHIO FILINGS:

Judgment,
filed 12/31/08 ..... C1 - C14

OTHER:

Private Placement Memorandum
[*Excerpts*] ..... D1 - D46

No. 08-3892

UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

UNITED STATES OF AMERICA,
Plaintiff-Appellee,

v.

MARK D. LAY,
Defendant-Appellant.

ORDER

BEFORE: GIBBONS, ROGERS, and KETHLEDGE, Circuit Judges.

The court having received a petition for rehearing en bane, which was circulated to all active judges of this court, none of whom requested a vote on the suggestion for rehearing en bane, the petition for rehearing has been referred to the original panel.

The panel has further reviewed the petition for rehearing and concludes that the issues raised in the petition were fully considered upon the original submission and decision of the case.
Accordingly, the petition is denied.

ENTERED BY ORDER OF THE COURT
S/ Leonard Green
Leonard Green, Clerk

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

UNITED STATES OF AMERICA,
Plaintiff-Appellee,

v. No. 08-3892

MARK D. LAY,
Defendant-Appellant.

Appeal from the United States District Court
for the Northern District of Ohio at Cleveland.
No. 07-00339-001-David D. Dowd, District Judge.

Argued: April 27, 2010

Decided and Filed: July 14, 2010

Before: GIBBONS, ROGERS, and KETHLEDGE,
Circuit Judges.

COUNSEL

ARGUED: Michael L. Cioffi, BLANK ROME LLP, Cincinnati, Ohio, for Appellant. Antoinette T. Bacon, ASSISTANT UNITED STATES ATTORNEY, Cleveland, Ohio, for Appellee. **ON BRIEF**: Michael L. Cioffi, Nathaniel R. Jones, Rachel L. Payne, BLANK ROME LLP, Cincinnati, Ohio, for Appellant. Antoinette T. Bacon, Laura McMullen Ford, ASSISTANT UNITED STATES ATTORNEY, Cleveland, Ohio, for Appellee.

ROGERS, J., delivered the opinion of the court, in which GIBBONS, 1., joined. KETHLEDGE,J. (pp. 12-13), delivered a separate opinion concurring in part and dissenting in part.

OPINION

ROGERS, Circuit Judge. Defendant Mark D. Lay appeals his fraud convictions related to a hedge fund investment by the Ohio Bureau of Workers' Compensation. Lay primarily argues that the jury instructions were improper and that insufficient evidence supports the jury's verdict because, as a hedge fund adviser, Lay had a fiduciary relationship only with the hedge fund, not with its investors. Lay also seeks a new trial based on three of the district court's evidentiary rulings and its restitution and forfeiture determinations. Because a hedge fund adviser can, in some circumstances, have a fiduciary relationship with an investor, the jury instructions were correct and sufficient evidence supports Lay's conviction. We also reject Lay's challenges to the district court's evidentiary rulings and its restitution and forfeiture determinations.

I. Background

The facts of this case–based on the indictment and the evidence presented by the Government in support of the allegations in the indictment–are set out in careful detail in the district court's opinion denying Lay's motion for judgment of acquittal. *United States v. Lay*, 566 F. Supp. 2d 652,655-68 (N.D. Ohio 2008). A brief summary is sufficient here. In 1992 Lay began serving as investment adviser to the Ohio Bureau of Workers' Compensation when Lay's company, Capital Management, Inc., began managing the Bureau's investment in a long-term bonds fund, the Long Fund. The Bureau remained Lay's client as to its Long Fund investment from 1992 onward. In 1998, Lay founded the Active Duration Fund, a hedge fund. In September of 2003, the Bureau shifted $100 million from the Long Fund to the Active Duration Fund. The hedge fund agreement governing the Bureau's Active Duration Fund investment set a non-binding 150% leveraging guideline, but in fact Lay consistently leveraged Active Duration Fund assets far over 150%. In March of 2004, the Active Duration Fund lost $7 million. In May of 2004, after Bureau officials discussed the loss with Lay, the Bureau invested an additional $100

million in the Active Duration Fund. The Active Duration Fund's value continued to decline. In September of 2004, the Bureau invested an additional $25 million in that fund to avoid losing its entire investment, and then terminated its interest in the fund. The Bureau recovered only about $9 million from its $225 million Active Duration Fund investment.

A federal grand jury indicted Lay on one investment adviser fraud count and multiple mail and wire fraud counts. The investment adviser fraud count tracked the following Investment Advisers Act provisions, codified at 15 U. S. C. § 80b-6, which make it unlawful for an investment adviser to use the mails or the instrumentalities of interstate commerce

> (1) to employ any device, scheme, or artifice to defraud any client or prospective client;
> (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client;
> ....
> (4) to engage in any act, practice or course of business which is fraudulent, deceptive, or manipulative.

The Superseding Indictment charged that Lay acted to:

> (a) employ devices, schemes, and artifices to defraud, the client, the [Bureau] and thereby the [Active Duration Fund]; (b) engage in transactions, practices and courses of business which operated as a fraud and deceit upon, the client, the [Bureau] and thereby the [Active Duration Fund]; and (c) engage in any act, practice and course of business which was fraudulent, deceptive and manipulative, to wit: exercising leverage in excess of 150% in the [Active Duration Fund], in violation of the [hedge fund agreement], and concealing and failing to disclose to the full extent his exercise of leverage in excess of 150%.

The Superseding Indictment also alleged that Lay's conduct constituted mail fraud and wire fraud because Lay sent interstate emails, faxes, and trade confirmations to carry out these trades.

At trial, Terry Gasper, the Bureau's Chief Financial Officer and the person who initially decided to invest Bureau money in the Active Duration Fund, testified that his "understanding [of the Active Duration Fund and Long Fund investments] was that

if Mr. Lay felt that bond prices in general were going to decline. . . the [Active Duration Fund] would be used to hedge those bonds . . . so that if the bond market did, in fact, go down in value, we would make some money in the [Active Duration Fund] to offset the . . . unrealized losses we would have suffered in [the Long Fund]." Gasper indicated that his experience with Lay and the Long Fund was "one of the primary reasons" he invested in the Active Duration Fund, that he felt the Active Duration Fund investment was "very conservative" and "low risk," and that the Bureau was "simply diversifying the product under a current manager" when it invested Long Fund assets already under Lay's management in the Active Duration Fund. Gasper testified that in the first half of 2003, before the Bureau invested in the Active Duration Fund, Lay told Gasper that the Active Duration Fund "would be using leverage only to reflect the value of what he had in the fund" and that Gasper had viewed the 150% leveraging guideline in the hedge fund agreement as "a way to give [Lay] some flexibility in running money and moving monies around." Gasper testified that when the Bureau had invested a second $100 million in the Active Duration Fund, he had assumed that Lay was acting in "an appropriate fiduciary way . . . that the

leverage in the [Active Duration Fund] was exactly what we agreed to, that maximum of 150 percent of fund value."

James McLean, the Bureau's Chief Investment Officer, testified that he and Lay had agreed in April of 2004, after the initial $7 million loss and before the second $100 million investment, that "the fund was . . . intended to be more of a net positive rate of return fund . . . [meaning] that [Lay is] investing in high quality fixed income securities, and if they're yielding a rate of return of say five percent on an interest bearing basis, then that fund, all things being equal and nothing else being done, would earn a five percent rate of return." As to leverage, McLean testified that he and Lay agreed that the Active Duration Fund was "allowed to use a bit of leverage to take positions to enhance that five percent rate of return when [Lay saw] opportunities within the marketplace," but that with this "modest" leverage, "even if that account were to lose a little bit based upon the leveraging of a bet that [Lay] placed on the short position. . . you still earn one or two percent based upon the core of the hedge fund portfolio." Lay had regularly reported to McLean in writing regarding the Long Fund's performance, and these reports had included a one-line summary of the

Active Duration Fund's value under the heading "other assets."

FBI Special Agent Jeremy Durgin testified that, of the Bureau's $214 million total loss, approximately $212 million was due to trades that had leveraged Active Duration Fund assets over 150%. Durgin testified that Lay had begun leveraging those assets over 150% in early 2004, that two-thirds of Lay's Active Duration Fund trades involved leveraging over 150%, that over one-fifth of those trades involved leveraging over 1000%, and that some trades involved leveraging over 10,000%.

Over Lay's objection, the district court also permitted the jury to hear Lay's deposition testimony from a previous civil case. In that deposition, Lay repeatedly stated that his company, Capital Management, Inc., "was the investment adviser for the [Active Duration Fund]" and "provided a service to the [Active Duration Fund]." Lay also stated in that deposition that the Bureau was Capital Management, Inc.' s "client" and that "the Bureau, as a client, pays the fees."

The district court instructed the jury that, in order to find Lay guilty of investment adviser fraud, the Government had to prove "*each* element of *either* [15 U.S.C. §] 80b-6(1) *or* 80b-6(2) or 80b-6(4)." 566 F.

Supp. 2d at 692 (emphasis in original). With respect to §80b-6(1) & (2), the court instructed that

> In order to [establish that Lay committed investment adviser fraud under these provisions], the government must prove beyond a reasonable doubt that the [Bureau] was Mark Lay's client with respect to its investment in the. . . Active Duration Fund. . . .
>
> A client is an individual or entity which compensates an investment adviser to provide advice directly or through publications or writings about the value of securities or the advisability of investing in, purchasing, or selling securities. . . .
>
> It is for you to determine as a matter of fact whether Mark Lay had an investment adviser-client relationship with the [Bureau] with respect to its investment in the . . . Active Duration Fund. There are two possible outcomes of your determination on this issue.
>
> First, you could find that the government failed to prove beyond a reasonable doubt that Mark Lay had an investment adviser-client relationship with the [Bureau] with respect to its investment in the . . . Active Duration Fund.

> Second, you could find that the government [has] proved beyond a reasonable doubt that Mark Lay did have an investment adviser-client relationship with the [Bureau] with respect to the [Bureau's] investment in the. . . Active Duration Fund. You could make this finding in one of two ways. The Defendant does not dispute that he was the investment adviser and the [Bureau] was his client with respect to the Long Fund which continued throughout the period of time at issue in the Superseding Indictment. Therefore, you could find that: 1) Lay established a second investment adviser-client relationship with the [Bureau] and he was the investment adviser to the [Bureau] with respect to both the Long Fund and the. . . Active Duration Fund, or that 2) the investment adviser-relationship between Lay and the [Bureau] regarding the Long Fund was based on the investment of the monies in the Long Fund wherever it was invested and was not severed when Long Fund monies were invested in the ... Active Duration Fund.

Id. at 694-95.

The court also instructed with respect to § 80b-6(4) that if the jury found that the Bureau was not Lay's client with respect to the Active Duration Fund, the jury was to determine as a matter of fact whether Lay nonetheless had a fiduciary duty with regard to the Active Duration Fund. *Id.* at 696. The district court rejected Lay's objection to this instruction.

To find Lay guilty of mail or wire fraud, the district instructed the jury that it had to find beyond a reasonable doubt that (1) "there was a scheme to defraud;" (2) "[Lay] knowingly participated in the scheme;" (3) the scheme included a material representation or concealment of a material fact;" (4) "[Lay] had the intent to defraud;" and (5) "[Lay] used the mail or caused another to use the mail in furtherance of the scheme."

After deliberations began, the jury asked to rehear Lay's deposition testimony. The district court permitted a re-reading, but first cautioned the jury "not to accord undue influence to that testimony."

The jury found Lay guilty on all counts and found in a special verdict form that Lay had obtained $590,526.23 in proceeds from his mail and wire fraud offenses. Lay moved for judgment of acquittal and argued that insufficient evidence supported his

convictions because he did not owe the Bureau a fiduciary duty and the Bureau was not his client as to its Active Duration Fund investment. Lay also moved for a new trial based on, among other reasons, alleged error in the district court's jury instructions and its limiting instruction upon the re-reading of Lay's deposition testimony, and cumulative error.

The district court denied Lay's motion for judgment of acquittal. The court held that sufficient evidence supported the existence of a fiduciary relationship between Lay and the Bureau as to its Active Duration Fund investment because Lay had a pre-existing fiduciary relationship with the Bureau as to its Long Fund investment, the Bureau intended its Active Duration Fund investment to "provide Lay with flexibility and investment management alternatives for half of the [Long Fund] monies in order to reduce the overall risk to the [Bureau] monies under Lay's control," the Bureau was not a passive investor in the Active Duration Fund, the Bureau had "regular and direct" communication with Lay about the Active Duration Fund, and the Bureau was the sole shareholder in the Active Duration Fund. 566 F. Supp. 2d at 670-71. The district court denied Lay's motion for judgment of acquittal as to the mail and wire fraud counts. *Id.* at 671 n.56. The

district court also denied Lay's motion for a new trial and held that the jury instructions were proper, that the court had issued a proper limiting instruction before Lay's deposition testimony was re-read to the jury, and that no cumulative error had occurred. *Id.* at 672, 677-78, 678-79. The district court directed that $590,526.23 be forfeited and imposed $212 million in restitution. On appeal, Lay challenges the district court's jury instructions and its denial of his motions for judgment of acquittal and a new trial.

II. Jury-instruction and sufficiency-of-the-evidence challenges

A. Investment adviser fraud

Lay's central argument is that, as to the hedge fund, he owed no fiduciary duty to the Bureau. The duty of a hedge fund adviser, the theory goes, is to the hedge fund and cannot be to the various investors in the fund. If the theory is correct, then various instructions to the jury, permitting the jury to find such a fiduciary duty, were in error and, indeed, acquittal should have been ordered. The theory fails, however, for the reasons carefully stated by the district court below. *Id.* at 668-71. Permitting the jury to determine the existence of a fiduciary

relationship was proper and, on the facts of this case, a reasonable jury could find that Lay owed the Bureau a fiduciary duty with respect to the Active Duration Fund. Lay's challenges to the jury instructions and to the denial of the acquittal motion in this regard are therefore both without merit.

As explained by the district court, "there is evidence in the record that the characteristics of an adviser-client relationship were present between defendant and the [Bureau] regarding the [Active Duration Fund]." *Id.* at 670. Lay has never disputed that he had an investment adviser-client relationship–and therefore a fiduciary relationship–with the Bureau as to its Long Fund investment, and the evidence supports the conclusion that this relationship continued through the existence of the Active Duration Fund and encompassed the Bureau's Active Duration Fund investment. As Gasper testified, the Bureau invested in the Active Duration Fund to diversify existing investments, achieve positive returns regardless of market conditions, and increase returns above those the Bureau could achieve with the Long Fund alone. Capital Management, Inc.'s inclusion of the Active Duration Fund as "other assets" in its Long Fund reports indicates that the Active Duration Fund and

the Long Fund were part of a single investment strategy and therefore part of the Bureau's single relationship with Lay. Unlike a typical hedge fund investor, the Bureau was the only investor in the Active Duration Fund at the relevant time and the Bureau had an active role in its Active Duration Fund investment, as indicated by McLean's meetings with Lay regarding that investment. The jury could therefore reasonably find, as a matter of fact, that Lay owed the Bureau a fiduciary duty as to the Active Duration Fund investment.

Lay's categorical argument to the contrary is primarily based upon reading too much into the holding of the District of Columbia Circuit in *Goldstein v. SEC*, 451 F.3d 873 (D.C. Cir. 2006), regarding the Investment Advisers Act (IAA). That case precluded the Securities and Exchange Commission from treating all hedge fund investors as clients of a hedge fund adviser for purposes of circumventing a small-dealer registration exemption. The case did not hold that a hedge fund investor could never be a client of a hedge fund adviser, or be owed a fiduciary duty by one, for purposes of the criminal fraud provisions of the IAA.

In *Goldstein*, the D.C. Circuit considered an SEC rule change related to the IAA registration

exemption for investment advisers with fewer than fifteen clients in the past twelve months. *See id.* at 874. Under the SEC's prior rule, a hedge fund adviser's client for registration purposes was the fund, not the fund's investors. *Id.* at 876. Under the SEC's new rule, however, a hedge fund adviser's clients would include the fund's investors. *Id.* at 877. The court held that the SEC had not "adequately explained how the relationship between hedge fund investors and advisers justifies treating the former as clients of the latter" and vacated the new rule. *Id.* at 882. The court reasoned that, based on the IAA's definition of "investment adviser," a client relationship results when the investor receives investment advice directly from the adviser, and because hedge fund investors do not always receive direct investment advice from hedge fund advisers, the IAA does not support treating all hedge fund investors as clients of hedge fund advisers. *Id.* at 879. As the court stated, "[a hedge fund adviser] does not tell the *investor* how to spend his money; the investor made that decision when he invested in the [hedge] fund. Having bought into the fund, the investor fades into the background; his role is completely passive." *Id.* at 879-80.

Goldstein did not hold that no hedge fund adviser could create a client relationship with an investor, but rather held only that the SEC had "not justified treating *all* investors in hedge funds as clients." *Id.* at 883. The court noted that hedge funds are "usually structured as limited partnerships to achieve maximum separation between ownership and management" and that "the general partner manages the fund . . . for a fixed fee and a percentage of the gross profits from the fund" while "[t]he limited partners are passive investors and generally take no part in management activities." *Id.* at 876. The court acknowledged that "different classes of investors [may] have different rights or privileges with respect to their investments" and that "[i]f . . . certain characteristics present in some investor-adviser relationships. . . mark a 'client' relationship, then the [SEC] should have identified those characteristics and tailored its rule accordingly." *Id.* at 882-83. It was therefore entirely consistent with *Goldstein* for the district court in Lay's case to permit the jury to find as fact that Lay owed the Bureau a fiduciary duty with respect to the Active Duration Fund. The jury's finding that Lay was guilty of investment adviser fraud is also consistent with *Goldstein* because the relationship between the Bureau and

Lay as to the Active Duration Fund was not a typical hedge fund adviser-investor relationship.

This disposes of the bulk of Lay's arguments on appeal. Lay also argues that the 150% limit on leveraging served only as a guideline rather than a binding limitation. However, the leeway contemplated by the leveraging guideline's non-binding nature does not permit leveraging over 150% in two-thirds of trades and leveraging over 1,000% in one-fifth of trades. Therefore, the district court's jury instructions fairly and adequately submitted the issues and applicable law to the jury, *United States v. Mick*, 263 F.3d 553, 569 (6th Cir. 2001) (standard), and, viewing the evidence in the light most favorable to the Government, a rational trier of fact could have found Lay guilty of investment adviser fraud based on his misrepresentation of or failure to disclose his leveraging activity to his client, the Bureau, *Jackson v. Virginia*, 443 U.S. 307, 319 (1979) (standard).

B. Mail and wire fraud

Sufficient evidence also supports the jury's determination that Lay is guilty of mail and wire fraud. The evidence establishes that Lay used

interstate mail or wires in furtherance of a scheme or artifice to defraud with intent to deprive the Bureau of money when he misrepresented to the Bureau the extent of his overleveraging and omitted material information in his reports to the Bureau. *See United States v. Prince*, 214 F.3d 740, 747-48 (6th Cir. 2000) (elements of the offense). When Gasper invested Bureau money in the Active Duration Fund, he believed the investment was conservative because Lay had represented that he would leverage based on the 150% guideline, and Gasper increased the Bureau's Active Duration Fund investment based on the same belief; therefore, Lay's misrepresentations of his leveraging activity caused the Bureau to part with money. The trade confirmations, emails, and faxes through which Lay conducted the fraud satisfy the mailing and wiring requirements because these documents "were designed to lull the victims into a false sense of security, postpone their ultimate complaint to the authorities, and therefore make the apprehension of the defendants less likely than if no mailings had taken place." *United States v. Daniel*, 329 F.3d 480, 489 (6th Cir. 2003). Therefore, viewing the evidence in the light most favorable to the Govermnent, a rational trier of fact could have found Lay guilty of mail and wire fraud.

Moreover, the district court's jury instructions on mail and wire fraud were also proper, and–for the reasons set out above with regard to the IAA–the district court properly declined to instruct the jury that, as a matter of law, Lay owed the Bureau no fiduciary duty and that Lay therefore could not be convicted of mail and wire fraud.

III. New trial motion

Lay is not entitled to a new trial because the three challenged evidentiary rulings were correct, the district court correctly determined restitution and forfeiture, and no cumulative error occurred.

The record belies Lay's contention that the Government consistently called the Bureau Lay's "client" at trial or interchanged the words "investor" and "client." Lay's own counsel, during cross-examination of a Bureau official, solicited the most significant discussion of this nature. Lay cannot complain about the discussion elicited by his own counsel, and other isolated references to the Bureau as Lay's client as to its Active Duration Fund investment do not warrant a new trial.

Lay's deposition testimony from a previous case was admissible non-hearsay because it is an

admission by a party-opponent, Fed. R. Evid. 801(d)(2); *see United States v. Moffie*, 239 F. App'x 150, 156-57 (6th Cir. 2007), and the deposition was not rendered inadmissible because Lay opined therein that the Bureau was his client. A lay witness may testifY to a legal conclusion that "does not involve terms with a separate, distinct and specialized meaning in the law different from that present in the vernacular." *United States v. Sheffiy*, 57 F.3d 1419, 1426 (6th ir. 1995). Because "client" does not have a separate, distinct, and specialized meaning in the law different from its meaning in the vernacular, the district court correctly permitted the jury to hear Lay's deposition and Lay was not entitled to a new trial on this basis.

Before permitting the re-reading of Lay's deposition testimony, the district court properly cautioned the jury "not to accord undue influence to that testimony." Lay's additional requested instruction, that the jury was not to take the testimony out of context, was unnecessary because the entirety of Lay's deposition testimony was re-read to the jury. In *United States v. Epley*, 52 F.3d 571, 579 (6th Cir. 1995), we ruled that a district court had not abused its discretion in re-reading testimony to a jury, reasoning in part that the danger of the jury's

taking the testimony out of context was not present because the jury re-heard the entire testimony of the witness. Therefore Lay was not entitled to a new trial based on the district court's refusal to instruct the jury not to take the re-read deposition testimony out of context.

The district court correctly ordered that $590,526.23 be forfeited based on the amount the jury found to represent or to be traceable to proceeds that Lay obtained from his mail and wire fraud. *See* 18 U.S.C. §§ 981, 982. The district court also properly imposed $212 million in restitution because this amount reflects the Bureau's losses due to Lay's over-leveraging of Active Duration Fund assets. As we held in *United States v. Sosebee*, 419 F.3d 451, 461 (6th Cir. 2005), such "restitution orders are not affected by the Supreme Court's ruling in *Apprendi v. New Jersey*, 530 U.S. 466 (2000), because the restitution statutes do not specify a statutory maximum." Therefore, Lay was not entitled to a new trial on this basis.

Finally, because Lay's individual claims of error fail, Lay was not entitled to a new trial based on cumulative error.

IV. Conclusion

For the foregoing reasons, the judgment of the district court is affirmed.

CONCURRING IN PART, DISSENTING IN PART

KETHLEDGE, Circuit Judge, concurring in part and dissenting in part. I join all but part II.B of the court's opinion. I dissent from that part because I do not think the government proved a case of mail fraud.

That is not to say it could not have. The government had ample proof that Lay defrauded the Bureau by misrepresenting his intentions with respect to the 150% leverage limitation, and that he did so in order to induce the Bureau to part with its money. The only remaining element of mail fraud was an interstate mailing "in furtherance of the scheme[.]" *United States v. Prince*, 214 F.3d 740, 748 (6th Cir. 2000); *see also* 18 U.S.C. § 1341 (a mailing must be "for the purpose of executing such scheme or artifice" to defraud). Given the abundance of proof as to Lay's misrepresentations generally, one might expect simply to see proof that one of them was mailed.

But we do not see that. Instead, the charged mailings are "trade confirmation slips," which one bank mailed to another as a result of trades that Lay authorized for the Active Duration Fund. No one

contends that the slips themselves contained any misrepresentations or that they played any role whatever in parting the Bureau from its money. Instead, the slips simply confirmed trades that Lay had made on the open market. The question, then, is whether the government proved the slips somehow furthered the fraud.

The government's explanation of this point is amorphous at best. It observes, correctly, that post-fraud mailings can further the scheme if "designed to lull the victims into a false sense of security, postpone their ultimate complaint to the authorities, and therefore make the apprehension of the defendants less likely than if no mailings had taken place." *United States v. Lane*, 474 U.S. 438, 451 (1986) (internal quotation marks omitted); *see also* Majority Op. at 10. The government contends the slips had this effect because they ensured that the Fund would not be assessed a five-percent penalty for failed trades. Had those penalties been assessed, the government says, Lay would have "lost [the Bureau's] confidence and business." Gov't Br. at 52. The government's explanation more or less trails off there; but we are left to infer, apparently, that had the Bureau lost confidence in Lay, it would have begun asking questions, whose answers might have

led to still other questions, which in turn could have uncovered the fraud. So, in the government's view, the slips furthered the scheme.

The question is one of degree. In my view, the bank slips were too remote from the antecedent fraud, and too speculative in their effects, to support a finding that they were "designed to lull the victims into a false sense of security[.]" *Lane*, 474 U.S. at 451. If the slips here were so designed, so too were Lay's annual submissions to the SEC to retain his status as a registered investment advisor, *see* 17 C.F.R. § 275.204-1; since absent that status the Bureau surely would have lost confidence in him. That is an awfully broad conception of mailings in furtherance of the fraudulent scheme. At some point the element exists only in theory, rather than in fact.

That said, I agree with the majority's affirmance of Lay's conviction for conspiracy to commit mail fraud and wire fraud. On that charge, the government did identify an overt act that concealed the fraudulent scheme from the Bureau. And my agreement on the conspiracy charge means that, even under my proposed disposition of this case, Lay's sentence would remain the same. The district court sentenced Lay to 60 months for the investment-adviser conviction, and 144 months for

each of the other convictions–including the conspiracy one–with all sentences running concurrently. Even absent the mail-fraud convictions, therefore, Lay's sentence would be 144 months. Thus, while I respectfully dissent from the majority's affirmance of Lay' s mail-fraud convictions, I join its affirmance of his sentence.

But my point, in closing, remains a practical one: The government would make its task easier in mail- and wire-fraud cases ifit would choose, as its charged communication, a blood relative of the fraud, rather than a second cousin by marriage. Reasonable jurists can disagree as to the outcome in cases like this one. But one wonders why they should have to.

For these reasons, I concur in part and dissent in part.

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No. 08-3892

UNITED STATES OF AMERICA,
Plaintiff - Appellee,

v.

MARK D. LAY,
Defendant - Appellant.

Before: GIBBONS, ROGERS, and KETHLEDGE, Circuit Judges.

JUDGMENT

On Appeal from the United States District Court for the Northern District of Ohio at Cleveland.

THIS CAUSE was heard on the record from the district court and was argued by counsel.

IN CONSIDERATION WHEREOF, it is ORDERED that the judgment of the district court is AFFIRMED.

ENTERED BY ORDER OF THE COURT
S/ Leonard Green
Leonard Green, Clerk

AO 245B (Rev. 06/05) Judgment in a Criminal Case

United States District Court
Northern District of Ohio

UNITED STATES OF AMERICA

v.

Mark D. Lay

Case Number:
1:07CR00339-001

USM Number:
55409-060

Richard M. Kerger and
Percy Squire
Defendant's Attorney

***AMENDED**
(to correct restitution amount)
JUDGMENT IN A CRIMINAL CASE

THE DEFENDANT:

X was found guilty on count(s) 1 and 4 of the Superseding Indictment after a plea of not guilty.

The defendant is adjudicated guilty of these offense(s):

Title & Section	Nature of Offense	Offense Ended	Count
15 USC Section 80b-6 & 80b-17	Investment Advisory Fraud	January 2005	1
18 USC Section 1349	Conspiracy to Commit or Attempt Mail & Wire Fraud	January 2005	2
18 USC Section 1341 & 2	Mail Fraud, Aiding & Abetting	January 2005	3 & 4

The defendant is sentenced as provided in pages 2 through 6 of this judgment. The sentence is imposed pursuant to the Sentencing Reform Act of 1984.

IT IS ORDERED that the defendant shall notify the United States Attorney for this district within 30 days of any change of name, residence, or mailing address until all fines, restitution, costs, and special assessments imposed by this judgment are fully paid. If ordered to pay restitution, the defendant must notify the court and the United

States Attorney of material changes in the defendant's economic circumstances.

July 8, 2008
Date of Imposition of Judgment

s/ David D. Dowd, Jr.
Signature of Judicial Officer

DAVID D. DOWD. JR.,
United States Senior District Judge
Name & Title of Judicial Officer

July 11, 2008
Date

IMPRISONMENT

The defendant is hereby committed to the custody of the United States Bureau of Prisons to be imprisoned for a term of 60 months as to Count 1 and 144 Months as to each of Counts 2, 3 and 4, and all counts to run concurrently with each other.

[X] The defendant is remanded to the custody of the United States Marshal.

RETURN

I have executed this judgment as follows:

_____

_____

Defendant delivered on _____ to _____

_____ at _____ with a certified copy of this judgment.

_____

UNITED STATES MARSHAL

By _____

Deputy U.S. Marshal

SUPERVISED RELEASE

Upon release from imprisonment, the defendant shall be on supervised release for a term of 3 Years.

The defendant must report to the probation office in the district to which the defendant is released within 72 hours of release from the custody of the Bureau of Prisons.

The defendant shall not commit another federal, state, or local crime.

The defendant shall not unlawfully possess a controlled substance. The defendant shall refrain from any unlawful use of a controlled substance. The defendant shall submit to one drug test within 15 days of release from imprisonment and at least two periodic drug tests thereafter, as determined by the Court.

[] The above drug testing condition is suspended, based on the court's determination that the defendant poses a low risk of future substance abuse. (Check, if applicable.)

[] The defendant shall not possess a firearm, ammunition, destructive device, or any other dangerous weapon. (Check, if applicable.)

[X] The defendant shall cooperate in the collection of DNA as directed by the probation officer. (Check, if

applicable.)

[] The defendant shall register with the state sex offender registration agency in the state where the defendant resides, works, or is a student, as directed by the probation officer. (Check, if applicable.)

[] The defendant shall participate in an approved program for domestic violence. (Check, if applicable.)

If this judgment imposes a fine or restitution, it is a condition of supervised release that the defendant pay in accordance with the Schedule of Payments sheet of this judgment.

The defendant must comply with the standard conditions that have been adopted by this court as well as with any additional conditions on the attached page.

STANDARD CONDITIONS OF SUPERVISION

1) the defendant shall not leave the judicial district without the permission of the court or probation officer;
2) the defendant shall report to the probation officer and shall submit a truthful and complete written report within the first five days of each month;
3) the defendant shall answer truthfully all inquiries by the probation officer and follow the instructions of the probation officer;

4) the defendant shall support his or her dependents and meet other family responsibilities;

5) the defendant shall work regularly at a lawful occupation, unless excused by the probation officer for schooling, training, or other acceptable reasons;

6) the defendant shall notify the probation officer at least ten days prior to any change in residence or employment;

7) the defendant shall refrain from excessive use of alcohol and shall not purchase, possess, use, distribute, or administer any controlled substance or any paraphernalia related to any controlled substances, except as prescribed by a physician;

8) the defendant shall not frequent places where controlled substances are illegally sold, used, distributed, or administered;

9) the defendant shall not associate with any persons engaged in criminal activity and shall not associate with any person convicted of a felony, unless granted permission to do so by the probation officer;

10) the defendant shall permit a probation officer to visit him or her at any time at home or elsewhere and shall permit confiscation of any contraband observed in plain view of the probation officer;

11) the defendant shall notify the probation officer within seventy-two hours of being arrested or questioned by a law enforcement officer;

12) the defendant shall not enter into any

agreement to act as an informer or a special agent of a law enforcement agency without the permission of the court; and

13) as directed by the probation officer, the defendant shall notify third parties of risks that may be occasioned by the defendant's criminal record or personal history or characteristics and shall permit the probation officer to make such notifications and to confirm the defendant's compliance with such notification requirement.

SPECIAL CONDITIONS OF SUPERVISED

The defendant shall provide the probation officer access to all requested financial information.

The defendant shall not incur new credit charges or open additional lines of credit without the approval of the probation officer.

The defendant shall apply all monies received from income tax refunds, lottery winnings, judgments, and/or other anticipated or unexpected financial gains to the outstanding court-ordered financial obligation.

The defendant is ordered to forfeit to the United States the sum of $590,526.23.

CRIMINAL MONETARY PENALTIES

The defendant must pay the total criminal monetary penalties under the Schedule of Payments on Sheet 6.

	Assessment	Fine	Restitution
TOTALS	$400.00	$0.00	$212,967,084.76

_____ The determination of restitution is deferred until ___. An Amended Judgment in a Criminal Case (AO 245C) will be entered after such determination.

_____ The defendant must make restitution (including community restitution) to the following payees in the amount listed below.

If the defendant makes a partial payment, each payee shall receive an approximately proportioned payment, unless specified otherwise in the priority order or percentage payment column below. However, pursuant to 18 U.S.C. § 3664(I), all nonfederal victims must be paid before the United States is paid.

Name of Payee	Total Loss*	Restitution Ordered	Priority of Percentage

Ohio Bureau of
Worker's Compensation
30 West Spring Street L-24
Columbus, OH 43215
Attention: Tracy L. Valentino,
Chief Fiscal & Planning Officer

TOTALS * $22,967,084.76

_____ Restitution amount ordered pursuant to plea agreement $ _____

_____ The defendant must pay interest on restitution and a fine of more than $2,500, unless the restitution or fine is paid in full before the fifteenth day after the date of the judgment, pursuant to 18 U.S.C. § 3612(f). All of the payment options on the Schedule of Payments sheet may be subject to penalties for delinquency and default, pursuant to 18 U.S.C. § 3612(g).

_____ The court determined that the defendant does not have the ability to pay interest and it is ordered that:

____ the interest requirement is waived for the _____ fine _____ restitution.

____ the interest requirement for the ____ fine ____ restitution is modified as follows:

*Findings for the total amount of losses are required under Chapters 109A, 110, 110A, and 113A of Title 18 for offenses committed on or after September 13, 1994, but before April 23, 1996.

SCHEDULE OF PAYMENTS

Having assessed the defendants ability to pay, payment of the total criminal monetary penalties are due as follows:

A [] Lump sum payment of $_____ due immediately, balance due

[] not later than _____ or
[] in accordance [] C, [] D, [] E, or [] F below; or

B [X] Payment to begin immediately (may be combined with [] C, [] D, [] E, or [X] F below; or

C [] Payment in equal installments of $___ over a period of __ , to commence __ days after the date of this judgment; or

D [X] The defendant shall pay 25% of defendant's gross income per month, through the Federal Bureau of Prisons Inmate Financial Responsibility Program. If a restitution balance remains upon release from imprisonment, payment is to commence no later than 60 days following release from imprisonment to a term of supervised release in equal monthly payments, or a least a minimum of 20% of defendant's gross monthly income during the term of supervised release and thereafter as prescribed by law. Notwithstanding establishment of a payment

schedule, nothing shall prohibit the United States from executing or levying upon property of the defendant discovered before and after the date of this Judgment.

E [] Payment during the term of supervised release will commence within _ (e.g., 30 or 60 days) after release from imprisonment. The court will set the payment plan based on an assessment of the defendant's ability to pay at that time; or

F [X] Special instructions regarding the payment of criminal monetary penalties:

[X] A special assessment of $400.00 is due in full immediately as to count(s) 1 through 4. PAYMENT IS TO BE MADE PAYABLE AND SENT TO THE CLERK, U.S. DISTRICT COURT

[] After the defendant is release from imprisonment, and within 30 days of the commencement of the term of supervised release, the probation officer shall recommend a revised payment schedule to the Court to satisfy any unpaid balance of the restitution. The Court will enter an order establishing a schedule of payment.

Unless the court has expressly ordered otherwise, if this judgment imposes imprisonment, payment of criminal monetary penalties is due during

imprisonment. All criminal monetary penalties, except those payments made through the Federal Bureau of Prisons' Inmate Financial Responsibility Program, are made to the clerk of the court.

The defendant shall receive credit for all payments previously made toward any criminal monetary penalties imposed.

[] Joint and Several (Defendant names, Case Numbers, Total Amount, Joint and Several Amount, and corresponding payee.)

[] The defendant shall pay the cost of prosecution.

[] The defendant shall pay the following court cost(s):

[] The defendant shall forfeit the defendant's interest in the following property to the United States:

Payments shall be applied in the following order: (1) assessment, (2) restitution principal, (3) restitution interest, (4) fine principal, (5) fine interest, (6) community restitution, (7) penalties, and (8) costs, including the cost of prosecution and court costs.

Copy No.: _____
Issued to: _____

CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM

MDL ACTIVE DURATION FUND, LTD.

(An exempted mutual fund company incorporated with limited liability under the laws of Bermuda)
Offering of Non-Voting, Redeemable, Participating Shares
Minimum Subscription Per Investor: U.S. $1,000,000
MDL CAPITAL MANAGEMENT, INC.
Investment Adviser
OLYMPIA CAPITAL INTERNATIONAL, INC.
Administrator

THESE SECURITIES ARE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER APPLICABLE LAW AND UNDER THE PROVISIONS OF THE FUND'S GOVERNING DOCUMENTS.

THE DATE OF THIS MEMORANDUM IS SEPTEMBER 22, 2003

LEGENDS

PROSPECTIVE SUBSCRIBERS IN THE FUND SHOULD INFORM THEMSELVES AS TO

THE LEGAL REQUIREMENTS AND TAX CONSEQUENCES WITHIN THE COUNTRIES OF THEIR RESIDENCE AND DOMICILE FOR THE ACQUISITION, HOLDING OR DISPOSAL OF SHARES AND ANY FOREIGN EXCHANGE RESTRICTIONS WHICH MAY BE RELEVANT TO THEM. IF YOU ARE IN ANY DOUBT ABOUT THE CONTENTS OF THIS MEMORANDUM, YOU SHOULD CONSULT YOUR STOCKBROKER, SOLICITOR, ACCOUNTANT OR OTHER FINANCIAL ADVISER.

NEITHER MDL ACTIVE DURATION FUND, LTD. (THE "FUND") NOR THE PARTICIPATING SHARES OF THE FUND (THE "SHARES") DESCRIBED IN THIS MEMORANDUM (THIS "MEMORANDUM") HAVE BEEN OR WILL BE REGISTERED OR QUALIFIED UNDER THE SECURITIES LAWS OF THE UNITED STATES ("U.S.") OR ANY OTHER JURISDICTION. THIS MEMORANDUM SHALL NOT CONSTITUTE AN OFFER TO SELL OR THE SOLICITATION OF AN OFFER TO BUY, NOR SHALL THERE BE ANY SALE OF SHARES IN ANY JURISDICTION IN WHICH SUCH OFFER, SOLICITATION OR SALE IS NOT AUTHORIZED OR TO ANY PERSON TO WHOM IT IS UNLAWFUL TO MAKE SUCH OFFER, SOLICITATION OR SALE. THE DIRECT OR INDIRECT OWNERSHIP OF SHARES BY "RESTRICTED PERSONS" AS DEFINED IN THIS MEMORANDUM IS PROHIBITED. NO PERSON HAS BEEN AUTHORIZED TO MAKE ANY REPRESENTATIONS CONCERNING THE FUND OR THE SHARES WHICH ARE INCONSISTENT

WITH THOSE CONTAINED IN THIS MEMORANDUM, AND ANY SUCH REPRESENTATIONS SHOULD ACCORDINGLY BE TREATED AS UNAUTHORIZED AND MAY NOT BE RELIED WON BY THE RECIPIENT.

UPON THE INVESTMENT ADVISER'S REGISTRATION WITH THE UNITED STATES COMMODITY FUTURES TRADING COMMISSION, THIS FUND WILL TRADE IN FUTURES. PURSUANT TO AN EXEMPTION FROM THE COMMODITY FUTURES TRADING COMMISSION IN CONNECTION WITH POOLS WHOSE PARTICIPANTS ARE LIMITED TO QUALIFIED ELIGIBLE PARTICIPANTS, A CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM FOR THIS POOL IS NOT REQUIRED TO BE, AND HAS NOT BEEN, FILED WITH THE COMMISSION. THE COMMODITY FUTURES TRADING COMMISSION DOES NOT PASS WON THE MERITS OF PARTICIPATING IN A POOL OR WON THE ADEQUACY OR ACCURACY OF A CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM. CONSEQUENTLY, THE COMMODITY FUTURES TRADING COMMISSION HAS NOT REVIEWED OR APPROVED AND IS NOT EXPECTED TO REVIEW OR APPROVE THIS CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM.

CERTAIN TRANSACTIONS IN FINANCIAL FUTURES AND RELATED OPTIONS AND THE INVESTMENT AND/OR HEDGING STRATEGIES ASSOCIATED THEREWITH WILL NOT BE AVAILABLE TO THE FUND UNLESS AND UNTIL

CERTAIN REGISTRATIONS ARE OBTAINED. THE INVESTMENT ADVISER IS SUBMITTING APPLICATIONS FOR SUCH REGISTRATIONS BUT IS NOT OBLIGATED TO PURSUE OR OBTAIN ANY SUCH REGISTRATIONS.

THE PURCHASE OF SHARES IS SPECULATIVE AND INVOLVES A HIGH DEGREE OF RISK. THERE IS NO ASSURANCE THAT THE FUND WILL BE PROFITABLE. SEE THE SECTION ENTITLED "RISK FACTORS" WITHIN THIS MEMORANDUM FOR A DESCRIPTION OF CERTAIN RISKS INVOLVED IN THE PURCHASE OF SHARES.

THIS MEMORANDUM IS INTENDED SOLELY FOR THE USE OF THE PERSON TO WHOM IT HAS BEEN DELIVERED BY THE FUND FOR THE PURPOSE OF EVALUATING A POSSIBLE INVESTMENT BY THE RECIPIENT IN THE SHARES DESCRIBED HEREIN, AND IT IS NOT TO BE REPRODUCED OR DISTRIBUTED TO ANY OTHER PERSONS (OTHER THAN PROFESSIONAL ADVISERS OF THE PROSPECTIVE INVESTOR RECEIVING

THIS DOCUMENT FROM THE FUND). THIS DOES NOT CONSTITUTE AN OFFERING TO ANY MEMBER OF THE GENERAL PUBLIC OF BERMUDA.

All monetary amounts for Shares set forth herein are expressed in U.S. dollars.

INTRODUCTION

MDL Active Duration Fund, Ltd. (the "Company" or the "Fund"), is an exempted, open ended mutual fund company incorporated under Bermuda law with limited liability and with unlimited duration. The Fund has been formed specifically for the purpose of providing an investment vehicle through which United States tax-exempt institutional investors and non-U.S. persons ("Investors") can invest in a portfolio consisting primarily of U.S. Treasury notes and bonds, U.S. agency notes and bonds and corporate and mortgage-backed fixed income securities. The Fund's duration, maturity structure and overall quality rating will be adjusted periodically based on an assessment of certain macro-economic factors. The Fund will seek to capture significant gains during periods when interest rates are generally declining and will seek to protect principal during periods when rates are generally rising.

The Fund's investment adviser is MDL Capital Management, Inc., a Pennsylvania corporation ("MDL" or the "Investment Adviser"). The Investment Adviser will provide investment advisory services to the Fund and will be responsible for the overall management of the Fund's portfolio. The Investment Adviser is a registered as an investment adviser with the U.S. Securities and Exchange Commission (the "SEC") under the Investment Advisers Act of 1940 (the "Advisers Act"). The Fund's investment objective is to profit by investing in U.S. Treasury, U.S. government agency, corporate and

mortgage-backed fixed income securities, currencies, short-term equity positions, futures and option contracts.

The Fund's investment strategy will include the use of leverage. ***The Investment Adviser, in its sole and absolute discretion and authority as investment advisor to the Fund will ultimately identify and select investments for the Fund.*** The Fund is designed primarily for U.S. tax-exempt institutional Investors and non-U.S Investors. There can be no assurance that the Fund will achieve its objectives.

The Fund is offering (the "Offering") its non-voting, redeemable, participating shares (the "Shares"), subject to prior subscription and other conditions. The Fund has a target equity capitalization of $300 million (which may be increased or decreased in the discretion of the board of directors of the Company (the "Board of Directors")). The minimum initial subscription per Investor is U.S. $1,000,000, subject to reduction in the discretion of the Board of Directors of the Company. Initially, Shares will be offered at U.S. $1,000.00 per Share. After commencement of investing activities, Shares will be offered for sale at the Net Asset Value per share as of the close of business on the last business day of each quarter (and any other date approved by the Board of Directors). The Shares are offered only to non-United States persons and certain U.S. tax-exempt Investors which meet the definitions of "qualified purchaser" as defined in the Investment Company Act of 1940, as amended (the "Investment Company Act") and

Qualified Eligible Purchaser as defined in Regulation 4.7 of the Commodity Futures Trading Commission. The Fund reserves the right to reject any subscription in whole or in part.

The initial offering period shall commence on the earlier of the date of the publication of this Memorandum, and the date of the filing of this Memorandum with the Registrar of Companies in Bermuda on September 22, 2003 (the "Initial Offering Period") and will end on the earlier to occur of the acceptance of subscriptions in the aggregate amount of $3,000,000 or January 12, 2004 (the "Initial Closing Date").

TABLE OF CONTENTS

SUMMARY 1

SUMMARY OF THE TERMS OF THE OFFERING AND THE FUND 1

DIRECTORY OF NAMES AND ADDRESSES . . 10

INVESTMENT OBJECTIVE AND STRATEGY OF THE FUND 11

SPECIAL INFORMATION ON THE MASTER FUND/FEEDER FUND INVESTMENT STRUCTURE 12

MANAGEMENT AND ADMINISTRATION 13

DESCRIPTION OF THE ADVISORY AGREEMENT 16

CONFLICTS OF INTEREST 16

RISK FACTORS 17

DETERMINATION OF NET ASSET VALUE . . . 24

CHARGES TO THE FUND 26

SERIES OF SHARES 28

REDEMPTIONS AND DIVIDENDS 29

REGISTRATION AND TRANSFERS 30

TAX CONSIDERATIONS 31

EMPLOYEE BENEFIT PLAN CONSIDERATIONS 33

PLAN OF DISTRIBUTION 34

ELIGIBLE SUBSCRIBERS 35

STATUTORY AND GENERAL INFORMATION 36

DEFINITIONS 39

SUMMARY
SUMMARY OF THE TERMS OF THE OFFERING AND THE FUND

The following is a summary of certain information about the Fund and the offering of Shares made by means of this Confidential Private Placement Memorandum (the "Memorandum"). The summary is qualified in its entirety by the more complete information appearing elsewhere in the Memorandum, and is subject to the detailed provisions of the Fund's Governing Documents and the Subscription Agreement attached hereto as Exhibit A. The Offering is subject to prior sale, modification and withdrawal.

FUND OVERVIEW

The Fund

The Fund is a Bermuda exempted, open ended mutual fund company incorporated on May 20, 2002 with limited liability in Bermuda. The operation and management of the Fund are governed by its Memorandum of Association and Bye-Laws, copies of which are available from the Administrator (the "Governing Documents"). The Registered Office and principal place of business of the Fund is Williams House, 20 Reid Street, Hamilton, HM11, Bermuda. The Fund has been classified as a Bermuda Institutional Scheme under the Bermuda Monetary Authority Collective Investment Scheme Regulations of 1998, as amended (the "Regulations"), and will be subject to the provisions of such law.

Investment Adviser

The Investment Adviser of the Fund is MDL Capital Management, Inc., a Pennsylvania corporation. The Investment Adviser's principal shareholders are Mark D. Lay, Steven L. Sanders, Edward Adatepe and Safeguard Scientific, Inc. The Investment Adviser is registered with the U.S. Securities and Exchange Commission as an investment adviser. The Investment Adviser is registering to become licensed as a commodity pool operator ("CPO") with the Commodity Futures Trading Commission ("CFTC"). Upon receipt of such licenses, the Investment Adviser will be the pool operator of the Fund.

Board of Directors

The Fund is governed by its board of directors (the "Directors" or "Board of Directors"). The members of the Board of Directors are Mark D. Lay, Steven L. Sanders and Edward Adatepe, who are the principals of the Investment Adviser, and Oskar P. Lewnowski and Raymond Morrison of Olympia Capital International, Inc., the Fund's administrator.

The Master Fund

The Fund may at some point in the future choose to invest all or some portion of its assets in a centralized investment company, commonly known as a "master fund" (the "Master Fund") (the Fund being a "feeder fund"). Such an investment would also be managed by the Investment Adviser at that level, but at all times in accordance with the investment style and strategies of the Fund as described in this Memorandum. The Master Fund would be a

Bermuda limited liability entity or State of Delaware limited partnership or similar entity eligible to be treated as a "partnership" for U.S. income tax purposes. It is anticipated that the Master Fund, if established, would admit one or more additional Investor Members consisting of other investment funds organized by the Investment Adviser to participate in the portfolio of the Master Fund.

Investment Objectives

The investment objectives of the Fund shall be to concentrate on investments in U.S. Treasury notes and bonds, U.S. government agency notes and bonds and corporate and mortgage-backed fixed income securities to generate consistent positive returns and to achieve an investment return in excess of that from the investment grade, broad market debt securities reflected in the Lehman Brothers Government Credit Bond Index (the "Lehman Government Credit Index"). In particular, the Fund will seek to significantly outperform the Index during periods when interest rates are generally declining and will seek to protect principal during periods when rates are generally rising. The Fund will seek to meet these objectives through an "active duration" approach, *e.g.*, the Fund's portfolio will be constructed to take advantage of anticipated movements in yield curves as well as inter - sector spread relationships. The variation in the Fund's average duration will be based upon the Investment Adviser's projections as to overall trends in these variables based on analysis of U.S. and global macro-economic growth factors. The Fund's portfolio will

include publicly-traded, United States-issued government agency, corporate and mortgage-backed fixed income securities and U.S. money market instruments and short-term investment funds, guaranteed investment contracts, forward contracts and, following the Investment Adviser's registration as a CPO with the CFTC, interest rate futures, financial futures and options thereon. The investments of the Fund will also involve the purchase of long and short positions of equity and investments and positions in foreign currencies. It is anticipated that the assets of the Fund will sometimes be pledged or otherwise collateralized to obtain a certain degree of leverage. The investments will be selected by the Investment Adviser in a manner consistent with the investment return objectives established by the Investment Adviser from time to time consistent with prudent standards of diversification, liquidity, quality, volatility and portfolio turnover. There is no assurance that the Fund will achieve its objectives.

Administrator

Olympia Capital International, Inc. (the "Administrator"), a British Virgin Islands corporation with a managing office in Bermuda, serves as administrator to the Fund. The Administrator will provide various administrative services to the Fund, including the calculation of the Fund's Net Asset Value and Net Asset Value per Share, processing Share subscriptions and redemptions and maintaining the Fund's principal books and records.

Registrar and Transfer Agent
The Fund has appointed Winchester Fiduciary Services Limited, located in Hamilton, Bermuda, as registrar and transfer agent (the "Registrar and Transfer Agent"). The Registrar and Transfer Agent is wholly-owned by Winchester Global Trust Company Limited, an affiliate of the Administrator.

Custodian
The Fund has engaged Credit Suisse First Boston Corporation, a Massachusetts corporation, to serve as custodian of the Fund's assets (the "Custodian"). The Custodian will also act as the prime broker of the Fund.

Potential Advantages of the Fund
The Fund is designed to enable Investors to access investment and trading strategies that are not generally available to most investors; to participate in investment programs that differ from those of traditional portfolio management; to diversify their investment portfolios; and to benefit from the investment techniques and strategies of the Investment Adviser.

Leverage
The Fund is expected to leverage the Fund's investment portfolio as a means to increase yield and enhance total return. Up to 150% of the Fund's assets, at the time of investment, may be leveraged (*i.e.*, the combined value of borrowings and short positions). Leveraging will include, but is not limited to, short selling of securities, reverse repurchase

agreements, certain option and futures transactions plus any borrowings to leverage the Fund's assets. Although the use of leverage may enhance returns on the Fund's portfolio and increase the number of investments that may be made by the Fund, it may also substantially increase the risk of loss. The percentage included above is intended as a guideline and may be changed from time to time at the sole discretion of the Board of Directors.

THE OFFERING

The Shares

The Fund is offering up to 10,000,000 non-voting, redeemable participating shares, U.S. $0.001 par value (the "Shares"). The Fund's share capital consists of the Shares and 100 voting, non-participating, non-redeemable shares, U.S. $0.01 par value each (the "Management Shares"), which are held by the MDL Active Duration Purpose Trust, a trust formed under the laws of Bermuda (the "Purpose Trust"). Harrington Trust Limited, a Bermuda company, is the sole trustee of the Purpose Trust. See "MANAGEMENT AND ADMINISTRATION--The Purpose Trust."

Plan of Distribution

The Fund intends to sell Shares which will be denominated in U.S. Dollars. Each Share will be issued at a price of U.S. $1,000.00 during the Initial Offering Period. There is no assurance that the Fund will receive and accept the minimum aggregate subscription amount necessary to commence

investing. If subscriptions totaling at least $3,000,000 are not accepted by the Fund during the Initial Offering Period, the subscriptions will be returned with interest actually earned thereon.

Continuous Offering Period

If at least $3,000,000 in subscriptions are accepted, the Fund will commence investing operations. Subsequent to the Initial Offering Period, Shares will be offered at the Net Asset Value per Share as of the last Business Day of each calendar quarter (each, a "Valuation Date"). Shares purchased after the Initial Offer Period will be issued as of the next Business Day after the relevant Valuation Date (the "Subscription Date"). A Business Day shall mean a day on which banks are open for business in Bermuda and New York, other than a Saturday or Sunday. Such proceeds will be invested in the Fund for the benefit of the Investor at the next Investment Date. Fractional Shares will be issued and carried out to three decimal places.

Minimum Purchase; Subscription Period

The minimum initial subscription per Investor is $1,000,000. The minimum subscription for additional investments by an Investor shall be $500,000. Shares are offered directly by the Fund. The minimum subscription amount and the minimum additional subscription amount may be reduced by the Board in its sole discretion. To subscribe for Shares, an Investor must submit a Subscription Agreement (in the form attached hereto) to the Administrator. Subscription Agreements and consideration for the

Shares subscribed to must be received by the Administrator at least five Business Days before the intended Subscription Date for the subscription. Upon acceptance of the subscription, capital contribution for the Shares subscribed must be transmitted immediately to the Fund's subscription account. Cleared funds must be in the Fund's account by 5 p.m. (Bermuda time) at least three Business Days before the Subscription Date . Consideration for Shares must be paid for in cash, although the Directors may in their absolute discretion accept other forms of payment.

Eligible Subscribers

Generally, except with respect to Qualified U.S. Persons (as defined in (b) below), the Shares will not be offered for sale in the U.S. or its territories or possessions or to nationals thereof, persons resident therein or entities established under the laws thereof. Shares will be offered from time to time on a private basis only to a select number of institutional and individual investors which meet applicable regulatory requirements. The Shares may be purchased only by (a) individuals that are not citizens or residents of the United States or entities that are not organized under the laws of the United States ("Non-U.S. Persons"), and (b) U.S. Persons within the meaning of the U.S. Internal Revenue Code of 1986, as amended (the "Code"), that are subject to the U.S. Employee Retirement Income Security Act of 1974, as amended ("ERISA"), or are otherwise exempt from payment of United States Federal income tax, or an entity substantially all of

the ownership interests in which are held by entities exempt from payment of U.S. Federal income tax ("Qualified U.S. Persons"). Prospective shareholders who are Qualified U.S. Persons must also qualify as "qualified purchasers" under §2(a)(51) of the Investment Company Act and "qualified eligible participants" under CFTC Regulation 4.7. Non-U.S. Persons and Qualified U.S. Persons that are Qualified Purchasers and Qualified Eligible Participants are hereinafter referred to as "Qualified Holders." Shares may not be purchased or held by or for the account of Bermuda residents. The Board of Directors may reject any subscription for any reason, or for no reason, in their sole and absolute discretion.

Series of Shares

In order to ensure a more equitable allocation of the Incentive Fee (see "Fees and Expenses" below) among Investors investing in the Fund at different times during the calendar year, Shares issued as of separate Subscription Dates will be designated as Shares of separate series (each with its own Net Asset Value per Share) as follows: Shares issued on the first Subscription Date of a calendar year will be designated as Series 1 Shares. Shares issued on Subscription Dates that do not fall on the first Subscription Date of a calendar year will be designated as Shares of a consecutive series of Shares. To the extent that there is no Loss Carryforward with respect to a Series, such additional series of Shares will be converted into Series 1 Shares at the beginning of each calendar

year as described in more detail under "FEES AND EXPENSES".

FEES AND EXPENSES

Organization and Offering Expenses

The aggregate initial organization and offering expenses will be advanced by the Investment Adviser and will be reimbursed by the Fund at such times and in such amounts as requested by the Investment Adviser. Provided that the Fund commences investing activities, the Fund may treat its organizational costs and expenses in accordance with U.S. Generally Accepted Accounting Principles, although it may elect to modify its treatment of such costs and expenses to accommodate its practical needs, including without limitation, by amortizing such organizational costs and expenses over a period of up to 60 months. Subsequent offering expenses will be direct expenses of the Fund.

Operating Expenses

The Fund will bear its routine operational expenses, including legal, custodial, accounting, printing, and audit expenses, expenses related to the investments of the Fund's assets, including, without limitation, brokerage commissions, investment related travel expenses, interest expense and professional and consulting fees relating to particular investments, insurance premiums (if any), administrative, directors fees and expenses, expenses incurred with respect to furnishing the Shareholders with annual reports and other financial information, the

Administrator's and the Registrar and Transfer Agent's fees and annual Bermuda government fees. The Investment Adviser will bear all of its general overhead expenses in connection with its services to the Fund (and the Master Fund), including employee salaries and office and equipment costs. The Fund will also, at such time as it becomes a member of the Master Fund, indirectly bear its allocable share of expenses incurred by the Master Fund, which will consist primarily of brokerage commissions and other operating and investment expenses paid by the Master Fund.

Investment Adviser Compensation

The Investment Adviser will receive a quarterly management fee determined at a rate equal to 1% per annum of the Fund's Net Asset Value, accrued monthly and payable in arrears as of the end of each calendar quarter. It also will receive a quarterly incentive fee (the "Incentive Fee") equal, in the aggregate, to 20% of the increase in Net Asset Value of each series of Shares over the sum of (i) the Series' Net Asset Value as of the commencement of each calendar quarter plus (ii) the yield on the Fund's portfolio at a rate equal to the yield of the Lehman Government Credit Index for such period (the "Hurdle"). A Series of Shares will only be charged with an Incentive Fee if its Net Asset Value at the end of a quarter (prior to accrued Incentive Fees), if any, for the quarter is greater than (i) its Net Asset Value at the time of its initial subscription (or the Initial Closing Date, whichever is later) or (ii) its Net Asset Value at the time the last Incentive Fee was

charged against such Series, whichever is higher, plus the Hurdle (the "High Water Mark"). In the event that the Fund invests in the Master Fund, the Investment Adviser will not be entitled to a separate management or investment advisory fee as manager of the Master Fund but will be entitled to reimbursement for expenses incurred on behalf of the Master Fund.

In order to ensure that the Incentive Fee is charged only to Shares that have appreciated in value since their acquisition and to make sure that all Shares have the same Net Asset Value, the Fund will issue different series of Shares to investors who invest at different times to ensure that the Incentive Fee is charged only to Shares that have appreciated in value. See "CHARGES TO THE FUND-Calculation of Investment Adviser Compensation."

Deferral of Fees. The Investment Adviser may elect, prior to the commencement of the Fund's trading activities with respect to its first calendar year of trading and prior to the commencement of each calendar year thereafter, to defer for a period of up to ten years payment of all or any portion of its Management Fees and/or Incentive Fees earned with respect to that subsequent period.

Administration

For its services as the Fund's Administrator, the Fund will pay the Administrator fees in accordance with the Administration Agreement.

Registrar and Transfer Agent
For its services, the Registrar and Transfer Agent will receive a fee of U.S. $2,500 per annum and is entitled to reimbursement of actual out-of-pocket expenses incurred on behalf of the Fund.

Directors' Fees
Each Director who is not an officer or employee of the Investment Adviser receives a flat annual fee of U.S. $2,000 for serving in such capacity. The Directors shall be entitled to reimbursement from the Fund for reasonable out-of-pocket expenses incurred by them on behalf of the Fund.

Trustee Services
The Trustee of the Purpose Trust holding the Management Shares will be entitled to an acceptance fee of $1,500 and an annual trustee fee of $1,500 payable by the Fund.

Custody and Prime Brokerage Services
For its services as custodian of the Fund's assets and prime broker of the Fund, the Fund will pay the Custodian in accordance with the Custody Agreement.

SHAREHOLDER INFORMATION

Limited Liability
Shareholders will purchase Shares in the Fund with limited liability and cannot lose more than the amount of their investment and profits thereon.

Redemption of Shares

Shares may be redeemed at a Shareholder's option at the Net Asset Value per Share of the relevant Series as of any Valuation Date upon at least 15 Business Days prior written notice to the Fund. The Fund may compulsorily redeem the Shares of any Shareholder on at least ten days' prior written notice to such Shareholder at the sole and absolute discretion of the Directors of the Company or where the holding of such Shares may result in regulatory, pecuniary, legal, taxation or material administrative disadvantage to the Fund or its Shareholders. There is no redemption charge or penalty. The Fund will generally pay 95% of the redemption price within 30 Business Days of the effective date of the redemption without interest, and the balance promptly at such time as the Fund shall determine, at the discretion of the Board of Directors.

The Fund expects to pay the entire redemption price in cash, although it has the right to distribute marketable securities. A redemption notice, once given, may not be cancelled or rescinded without the consent of the Directors in their sole discretion.

The Fund reserves the right to decrease, limit, delay or deny a redemption request, or any payment on a redemption request, if reasonably necessary in order to comply with the Fund's credit and other agreements, as well as for other reasons.

Transfer of Shares
There is no active secondary trading market for the Shares, nor is one expected to develop. Shares may not be sold, transferred or otherwise disposed of by a Shareholder in the United States or to any person corporation or entity which is not a Qualified Holder without prior written consent of the Fund and compliance with all applicable laws.

Favorable Tax Treatment
Under existing legislation in Bermuda, there are no income, capital gains or withholding taxes payable by the Fund or its Shareholders, nor are there any Bermuda estate, succession, or inheritance taxes payable by the Shareholders with respect to their Shares.

There is, at present, no direct taxation in Bermuda and interest, dividends and gains payable to the Fund will be received free of all Bermuda taxes. The Fund is an exempted company under Bermuda law and the Fund has made application to the Minister of Finance of Bermuda for, and expects to receive, an assurance that no law hereafter enacted in Bermuda imposing any taxes or duty to be levied on income or capital assets, gains or appreciation will apply to any income or property of the Fund.

The Fund and its Shareholders should not be subject to United States taxation as a consequence of the Fund's trading activities.

Dividends and Distributions

The Fund is a capital appreciation fund and does not intend to distribute dividends. Any dividends declared will be in the sole discretion of the Directors and will be paid out of the Fund's accumulated net income plus the net of accumulated realized and unrealized capital gains and accumulated realized and unrealized capital losses. Any dividends declared will be paid in accordance with Bermuda law.

Net Asset Value

The Net Asset Value of the Fund and each Series will be calculated at each Valuation Date in U.S. Dollars (unless the calculation at such Valuation Date has, for any reason, been postponed or suspended). Shareholders may, at any time, obtain information from the Fund regarding the most recently available indication of Net Asset Value.

ERISA Considerations

Fiduciaries and other persons investing in Shares in the Fund on behalf of employee benefit plans, employee retirement plans, individual retirement arrangements, Keogh Plans and other plans (together, "Plans") subject to ERISA or the Code should be aware that the assets of the Fund may constitute "plan assets" for purposes of the reporting, disclosure, prohibited transaction and fiduciary responsibility provisions of ERISA and the Code. The Investment Adviser qualifies as a "qualified professional asset manager" under applicable regulations under ERISA and will take all appropriate steps to ensure that the Fund does not

engage in any prohibited transactions under ERISA. The Investment Adviser will be a fiduciary of Plans investing in the Fund for purposes of ERISA. An investment in the Fund by Plan Investors requires special considerations, and fiduciaries of such Plans are encouraged to carefully review this Memorandum and the Section entitled "ERISA Considerations."

GENERAL

Auditors
Deloitte & Touche, Hamilton, Bermuda

Legal Counsel
Foley & Lardner, Milwaukee, Wisconsin, have counseled the Investment Adviser on various matters of United States law relating to the Fund. Appleby, Spurling & Kempe, Hamilton, Bermuda, have advised the Investment Adviser and the Fund 67a on various matters of Bermudan law relating to the Fund.

Custody Arrangements
The Fund is exempt under the Regulations from the requirement to appoint a Bermuda custodian of Fund Assets since the Fund is classified as a Bermuda Institutional Scheme. The Custodian will serve as custodian of the assets of the Fund.

Prime Broker
The Custodian will also initially be engaged as prime broker for the Fund, will function as clearing agent and will provide margin leverage and certain

valuation and reporting services to the Fund and the Administrator.

Reports
The Fund will provide Investors with monthly unaudited performance reports and annual audited financial statements prepared by the Fund's auditors.

Fiscal Year
The Fund's fiscal year will be the calendar year ending December 31st.

Conflicts of Interest
The Fund will be subject to certain actual and potential conflicts of interest. For example, the Investment Adviser will not be required to devote all of its time to the management of the Fund and the Investment Adviser has provided and expects to continue to provide investment management and advice to clients other than the Fund. In addition, the terms of the Investment Adviser's compensation from the Fund was not established by arm's length negotiations. See "CONFLICTS OF INTEREST."

Risks
Investment in the Fund involves greater risks than certain other types of investments. Investors in the Fund should be able financially to bear a loss of their investment. There is no assurance that the Fund will be profitable or will avoid substantial losses. "See Risk Factors."

RISK FACTORS

There is high risk associated with an investment in the Fund and an investment in the Fund should only be made after consultation with independent qualified sources of investment and tax advice. The following does not purport to be a comprehensive summary of all the risks associated with an investment in the Fund. Rather, the following are only certain particular risks to which the Fund is subject that the Investment Adviser wishes to encourage prospective investors to discuss in detail with their professional advisors:

The Fund Has No Performance History. The Fund has no performance history.

Reliance on the Investment Adviser. All decisions with respect to the Fund's assets and the general management of the Fund will be made by the Investment Adviser which relies on the services of several key employees, including without limitation, Mark D. Lay, Steven L. Sanders and Edward Adatepe. Shareholders will have no right or power to take part in the management of the Fund. As a result, the success of the Fund for the foreseeable future will depend largely upon the ability of the Investment Adviser and in particular Mark D. Lay, Steven L. Sanders and Edward Adatepe. Should any of these employees leave or become incapacitated for any period of time, profitability of the Fund's investments may suffer.

Achievement of the Fund's Investment Objective. No guarantee or representation is made that the Fund's Investment Objective will be successful. The Fund's investment program may include such investment techniques as short sales, leverage and limited diversification, which practices can, in certain circumstances, maximize the adverse impact to which the Fund's investments may be subject.

Eligibility to Engage in Futures Transactions. Certain transactions in commodity futures and options on futures and the investment and trading strategies associated with such transactions will not be available to the Fund unless and until the Investment Adviser has registered as a CPO with the CFTC. While the Investment Adviser has filed an application with the CFTC for licensing as a CPO, no assurance can be given that such license will be obtained and the Investment Adviser is not obligated to pursue or obtain any such license or registration.

No Current Income. The Fund's investment policies should be considered speculative, as there can be no assurance that the Investment Adviser's assessments of the short-term or long-term prospects of investments will generate a profit. In view of the fact that it is unlikely that the Fund will pay dividends, an investment in the Fund is not suitable for investors seeking current income for financial or tax planning purposes.

Currency Risk. Investments in securities of non-U.S. issuers will be denominated in currencies other than

the U.S. Dollar, and hence the value of such investments will depend on the relative strength of the U.S. Dollar. The Fund may be affected favorably or unfavorably by exchange control regulation or changes in the exchange rate between foreign currencies and the U.S. Dollar. Changes in foreign currency exchange rates may also affect the value of dividends and interest earned, and the level of gains and losses realized on the sale of securities. The rate of exchange between the U.S. Dollar and other currencies is determined by forces of supply and demand in the foreign exchange markets. These prices are affected by the international balance of payments and other economic and financial conditions, government intervention, speculation and other factors. Additionally, because the Fund's Net Asset Value will be calculated, purchased and redeemed in U.S. Dollars, each shareholder, and not the Fund, will bear the risk of any currency exposure resulting from differences, if any, in the value of the U.S. Dollar relative to the shareholder's reference currency.

Investment in a Master Fund. An investment by the Fund in the Master Fund may be affected by an investment by other funds in the Master Fund. In view of the fact that all expenses of the Master Fund would be shared pro rata among its investors, if other investors in the Master Fund redeem their interests, the possibility exists that the Fund would bear the burden of an increased share of the Master Fund's expenses. Moreover, investors with larger investments than others may outvote the smaller

investors to their detriment. (See "SPECIAL INFORMATION ON THE MASTER FUND/FEEDER FUND INVESTMENT STRUCTURE.")

Counterparty Risk. The Fund is subject to the risk of the failure or default of any counterparty to the Fund's transactions. If there is a failure or default by the counterparty to such a transaction, the Fund will have contractual remedies pursuant to the agreements related to the transaction. The Fund seeks to minimize the Fund's counterparty risk through the selection of financial institutions and types of transactions employed. However, the Fund's currency hedging transactions and other operational mechanisms designed to match the Fund's maturity requirements to cash flow may involve counterparty and other risk elements that may create unforeseen exposures.

Nature of Certain Investments. There is no limitation on the size or operating experience of the companies in which the Fund may invest, provided that such securities have a Standard & Poor's rating of B or better. Some small companies in which the Fund may invest may lack management depth or the ability to generate internally or obtain externally the funds necessary for growth. Companies with new products or services could sustain significant losses if projected markets do not materialize. Further, such companies may have, or may develop, only a regional market for products or services and may be adversely affected by purely local events. Such companies may be small factors in their industries and may face intense

competition from larger companies and entail a greater risk than investment in larger companies.

Risks of Special Techniques Used by the Investment Adviser. The Fund may invest using special investment techniques that may subject the Fund's investments to certain risks. Certain, but not all, of these techniques and the risks that they entail are summarized below. The Fund, in any event, is not designed to correlate to the broad bond market, and should not be viewed as a substitute for conventional fixed income investments.

Investments in Fixed-Income Securities Generally. The prices of the Fund's fixed-income securities respond to economic developments, particularly interest rate changes, as well as to perceptions about the creditworthiness of individual issuers, including governments. Generally, the Fund's fixed- income securities will decrease in value if interest rates rise and vice versa, and the volatility of lower-rated securities is even greater than that of higher-rated securities. Also, longer-term securities are generally more volatile, so the average maturity or duration of these securities affects risk.

Although the Fund's U.S. government securities are considered to be among the safest investments, they are not guaranteed against price movements due to changing interest rates. Obligations issued by some U.S. government agencies are backed by the U.S. Treasury, while others are backed solely by the

ability of the agency to borrow from the U.S. Treasury or by the agency's own resources.

The Fund is also subject to the risk that its investment approach, which focuses on a broad range of fixed income instruments, may perform differently than other funds which target specific segments of the fixed-income market or invest in other asset classes.

Risks of Leverage. Borrowing money to purchase securities may provide the Investment Adviser with the opportunity for greater capital appreciation and to extend or shorten the average duration of the Fund's portfolio but, at the same time, will increase the Fund's exposure to capital risk and higher current expenses. The use of leverage also increases the volatility of the Fund's portfolio by magnifying both increases and declines in the value of the Fund's assets.

Up to 150% of the Fund's assets, at the time of investment, may be leveraged *(i.e.,* the combined value of borrowings and short positions). If the Fund's assets decline in value or there are significant redemptions from the Fund, the Fund may be required to post additional collateral with the lender or liquidate assets to pay off its borrowings. Moreover, if the assets under management are not sufficient to pay the principal of and interest on the debt when due, the Fund could sustain a total loss of its investment.

Investments in Mortgage-Backed Securities. Mortgages underlying mortgage-backed securities may be paid off early, particularly in periods when interest rates are low, which makes it difficult to determine the actual maturity of such securities and therefore to calculate how they will respond to changes in interest rates. The Fund may have to reinvest prepaid amounts of lower interest rates. The risk of prepayment is an additional risk of mortgage-backed securities.

Short Selling. The Fund may sell securities of an issuer short. If the price of the issuer's securities declines, the Investment Adviser may then cover the short position with securities purchased in the market. The profit realized on a short sale will be the difference between the price received in the sale and the cost of the securities purchased to cover the sale.

The possible losses from selling short a security differ from losses that could be incurred from a cash investment in the security; the former may be unlimited, whereas the latter can only equal the total amount of the cash investment. Short selling activities are also subject to restrictions imposed by the various national and regional securities exchanges, which restrictions could limit the investment activities of the Investment Adviser.

Risks of Options Trading. In seeking to enhance performance or hedge assets, the Investment Adviser may purchase and sell call and put options on both securities and securities indexes. A securities index

measures the movement of a certain group of securities by assigning relative values to the securities included in the index.

Both the purchasing and the selling of call and put options contain risks. Although an option buyer's risk is limited to the amount of the purchase price of the option, an investment in an option may be subject to greater fluctuation than an investment in the underlying securities. In theory, the exposure to loss is potentially unlimited in the case of an uncovered call writer (*i.e.*, a call writer who does not have and maintain during the term of the call an equivalent long position in the stock or other security underlying the call), but in practice the loss is limited by the term of existence of the call. The risk for a writer of an uncovered put option (*i.e.*, a put option written by a writer that does not have and maintain an offsetting short position in the underlying stock or other security) is that the price of the underlying security may fall below the exercise price.

The effectiveness of purchasing or selling securities index options as a hedging technique will depend upon the extent to which price movements in assets that are hedged correlate with price movements of the index selected. Because the value of an index option depends upon movement in the level of the index rather than the price of a particular security, whether a gain or loss will be realized from the purchase or writing of options on an index depends upon movements in the level of prices in the securities market generally, rather than movements

in the price of a particular security. Successful use of options on indexes will depend upon the ability of the Investment Adviser to predict correctly movements in the direction of the market generally. This ability requires skills and techniques different from those used in predicting changes in the price of individual securities.

Risks of Futures Trading. Upon licensing of the Investment Adviser by the CFTC as a CPO and satisfaction of certain other conditions, the Fund may acquire commodities futures contracts and options on futures contracts.

Futures contracts and options thereon are highly volatile. Price movements of financial and interest rate futures and options thereon are influenced by a wide variety of factors, including, among other things, government, trade, fiscal, monetary and exchange programs and policies, national and international political and economic events and changes in interest rates.

When futures contracts are traded on United States exchanges, both buyer and seller are required to post margins with the broker handling their trades as security for the performance of their purchase and sale undertakings and to offset losses in their trades due to daily fluctuations in the markets. The low margin deposits typically required in futures trading (typically between 2% and 15% of the value of the futures contracts) permit an extremely high degree of leverage. Accordingly, a relatively small change in

interest rates or the price of a commodity can produce a disproportionately large profit or loss, which can exceed substantially more than the initial margin on a trade. The Investment Adviser intends to limit the Fund's initial margin and option deposits in connection with such futures contracts to not more than 10% of the Fund's assets.

Successful use of futures by the Investment Adviser is also subject to the Investment Adviser's ability to predict correctly movements in the direction of interest rates and other relevant financial markets, and to the extent a transaction is entered into for hedging purposes, to ascertain the appropriate correlation between the transaction being hedged and the price movements of the futures contract.

Swap Agreements. The Fund may enter into interest rate, index or currency rate swap agreements in an attempt to hedge against changes in interest or currency rates or index values exceeding minimum or maximum values. Most swap agreements entered into by the Fund would calculate the obligation of the parties on a "net" basis. Consequently, the Fund's obligations or rights on a swap agreement, and the risk of loss, would be limited only to the net amount to be paid or received based on the relative values of the positions held by each party.

Portfolio Turnover. Because the Investment Adviser will make changes whenever necessary, in its opinion, to take advantage of anticipated movements in the U.S. Treasury yield curve and/or inter-sector

spread relationships, it is anticipated that the Fund's portfolio will have a high turnover rate. Turnover of the Fund's portfolio may involve the payment by the Fund of dealer spreads or underwriting commissions, and other transaction costs, on the sale of securities, as well as on the reinvestment of the proceeds in other securities. The greater the portfolio turnover, the greater the transaction costs to the Fund which will reduce the Fund's total return.

Lack of Diversification. The Fund's portfolio may not be diversified among sectors, industries, geographic areas, duration or types of securities. In addition, the Fund's portfolio may not be diversified among a wide range of issuers. Accordingly, the Fund's portfolio may be subject to a more rapid change in value than would otherwise be the case if the Fund were required to maintain a wide diversification of its investments.

Acquisition of Illiquid Securities. Fund investments may include significant amounts of debt securities and other financial instruments for which no market or only a limited market exists (and which may even be restricted as to transferability under federal or state securities laws), and the disposition of such investments in the event of an unsuccessful outcome may be possible only at substantial discounts from their purchase price or intrinsic business value. The Fund's holding of illiquid securities may adversely affect the ability of Shareholders to receive redemption proceeds.

Incentive Fee Arrangements. The Investment Adviser could receive substantial compensation if it generates increases in Net Asset Value above the Hurdle for the Shareholders. Such compensation may provide an incentive for the Investment Adviser to effect larger and more risky transactions than would be the case in the absence of such arrangements. The Investment Adviser does not expect to modify or adjust its investment methodology in any way as a result of such incentive. The Investment Adviser may receive compensation with respect to unrealized appreciation of Fund assets as well as with respect to realized gains.

Advisers Act Prohibition. Section 205(a)(1) of the Advisers Act prohibits investment advisers, unless exempted from registering as an investment adviser under the Advisers Act, from providing investment advice for compensation "on the basis of a share of capital gains upon or capital appreciation of the funds or any portion of the funds of [a] client." The Investment Adviser will provide investment advice to the Fund and will be compensated, in part, upon a share of the capital gains of the Fund.

In order to prevent a possible violation of Section 205(a)(1) of the Advisers Act, the Fund will seek to comply with Rule 205-3 (the "Rule") under the Advisers Act, which permits an investment adviser to collect fees on a capital gains basis if such advice is provided solely to "qualified clients" as defined under the Rule. Since all Investors must be "Qualified Purchasers" in order to invest in the Fund and a

Qualified Purchaser also satisfies the criteria for a Qualified Client, the Fund will be in compliance with the Rule.

The intended purpose behind the Advisers Act prohibition of such fee arrangements with clients (unless the client is a "qualified client") is the belief that this type of performance fee arrangement may create an incentive for the Investment Adviser to make investments that are riskier or more speculative than would be the case in the absence of a performance fee.

Non-Public Information. From time to time, the Investment Adviser may come into possession of material non-public information regarding a potential investment that limits the Investment Adviser's flexibility in buying and selling Fund investments. The Fund's investment flexibility may be constrained as a consequence of the Investment Adviser's inability to use such information for investment purposes.

Broker-Dealers. All orders for the purchase or sale of Fund investments will be placed on behalf of the Fund by the Investment Adviser. The Investment Adviser may negotiate the purchase of investments directly with the sellers or may utilize broker-dealers to execute transactions. In selecting broker-dealers, subject to applicable limitations of the federal securities laws, the Investment Adviser will consider such factors as size and type of the transaction, the nature and character of the markets for the security,

the quality of the execution and settlement services, the financial condition of the broker-dealer firm and the reasonableness of any commissions.

The Fund may execute portfolio transactions with broker-dealers who provide research and/or execution services to the Fund and/or other accounts over which the Investment Adviser or its affliates exercise investment discretion. The selection of such broker-dealers generally is made by the Investment Adviser based upon the quality of such research and/or execution services. In any case where the Fund is to pay higher commissions in recognition of such research and/or execution services, the Investment Adviser must determine in good faith that such commissions are reasonable in relation to the value of the brokerage and/or research service viewed in terms of a particular transaction for the Investment Adviser's overall responsibilities to the Fund or its other clients.

Custodial Risks of Broker/Dealers. Various broker/dealers will trade with the relevant exchange as a principal on behalf of the Fund, in a "debtor-creditor" relationship, unlike other clearing broker relationships where the broker is merely a facilitator of the transaction. Such broker could, therefore, have title to certain assets of the Fund (for example, the transactions which the broker has entered into on behalf of the Fund as principal as well as the margin payments which the Fund provides). In the event of such broker's insolvency, the transactions which the broker has entered into as principal could therefore

default and such assets of the Fund could become part of the insolvent broker's estate, to the detriment of the Fund.

Early Termination. In the event of the early termination of the Fund, the Fund would have to distribute to the Shareholders their pro rata interest in the assets of the Fund. Such an early termination would have the effect of accelerating the unamortized portion of any organizational fees, thereby decreasing amounts otherwise available for distribution. Certain assets held by the Fund may be illiquid and might have little or no marketable vale. It is possible that at the time of such sale or distribution, certain securities held by the Fund would be worth less than the initial cost of such securities, resulting in a loss to Shareholders.

Effect of Substantial Withdrawals. Substantial withdrawals by Shareholders within a short period of time could require the Investment Adviser to liquidate positions more rapidly than would otherwise be desirable, which could adversely affect the value of the Fund's assets. The resulting reduction in the Fund's assets could make it more difficult to generate a positive rate of return or to recoup losses due to a reduced equity base.

Regulation. The Fund is not registered as an investment company under the Investment Company Act (or any similar state laws). Registered investment companies are subject to extensive regulation. Investors, therefore, will not be accorded

the protective measures provided by such legislation. The Fund is governed by Bermuda law. Under Bermuda law, the Directors' principal duty is to act in the best interests of the Company. Shareholders may therefore not have the same statutory protection or remedies available under the laws of other jurisdictions.

Changes in Regulatory Requirements. The Fund's investments will be subject to various Federal, state and local regulatory requirements. Failure to comply with these requirements could result in the imposition of fines by governmental authorities or awards of damages to private litigants. Further, the Securities and Exchange Commission ("SEC") recently announced that it has commenced a review of "hedge funds" *(i.e.,* unregistered and unregulated investment entities like the Fund) to determine if it is necessary to enhance regulation of such entities for investor protection purposes. In the event that new regulations are adopted that require registration and/or impose other regulatory requirements under the securities laws for hedge funds, there can be no assurance that the Fund's operations would not be materially affected, in the form of increased costs and other regulatory requirements that could affect the potential return to investors in the Fund. There can be no assurance that these requirements will not require significant unanticipated expenditures by the Fund.

Conflicts of Interest. The Fund is subject to conflicts of interest. See "Conflicts of Interest."

Reserve for Contingent Liabilities. Under certain circumstances, the Board of Directors may find it necessary to establish a reserve for contingent liabilities or withhold a portion of the Shareholder's settlement proceeds at the time of redemption, in which case, the reserved portion would remain at the risk of the Fund's activities.

Risk of Litigation. The Fund may accumulate substantial positions in the securities of a specific company. Sometimes the Investment Adviser may engage in a proxy fight, become involved in litigation or attempt to gain control of a company. Under such circumstances, the Fund may be named as a defendant in a lawsuit or regulatory action and be subject to the costs involved.

Lack of Independent Experts Representing Investors. The Fund and the Investment Adviser have each consulted with counsel, accountants and other experts regarding the formation and terms of the Fund and the Advisory Agreement. The investors, however, have not been represented by such independent experts. Each prospective investor should consult his own legal, tax and financial advisers regarding the desirability of purchasing Shares and the suitability of an investment in the Fund. Foley & Lardner and Appleby, Spurling & Kempe are U.S. and Bermuda counsel to the Fund, respectively, and do not represent the prospective investors or Shareholders of the Fund.

Lack of Voting Rights. The Shares being offered participate in the profits and losses of the Fund but do not carry voting rights except under very limited circumstances. See "Statutory and General Information."

Limited Ability to *Liquidate Investment in Shares.* There is no public market for the transfer of Shares. A Shareholder may require the Fund to redeem all or any whole number of its Shares as of the close of business on any Valuation Date at their Net Asset Value. However, the right to obtain payment on redemption is contingent upon the receipt by the Fund of 15 Business Days' written notice, and the Redemption Price may differ significantly from the value of such Shares when redemption was requested. Requests for redemptions may not be withdrawn. The Fund may suspend any or all of the calculation of Net Asset Value, the calculation of Net Asset Value per Share and redemptions in the circumstances set out under "Redemptions and Transfers – Temporary Suspensions." The Fund may also temporarily suspend redemptions in order to effect an orderly liquidation of the Fund's assets necessary to effect redemptions.

The foregoing list of risk factors does not purport to be a complete explanation of the risks involved in an investment in the Fund. Potential investors should read this entire Memorandum before determining whether to invest in the Fund and

consult with their own financial and tax advisers. Potential investors should also be aware that, if they decide to purchase Shares, they will have no role in the management of the Fund, will not have any voting rights (except under very limited circumstances), and will be required to rely on the expertise of the Fund's Directors and the Investment Adviser in dealing with the foregoing (and other) risks on a day-to-day basis.

THE SHARES ARE SPECULATIVE AND INVOLVE A HIGH DEGREE OF RISK. THEY ARE SUITABLE ONLY FOR PERSONS WHO CAN AFFORD TO LOSE THEIR ENTIRE INVESTMENT. SHAREHOLDERS SHOULD READ THE MEMORANDUM AND ARTICLES OF ASSOCIATION AS WELL AS THE FUND'S CONTRACTS WITH SERVICE PROVIDERS WHICH ARE REFERENCED IN "STATUTORY AND GENERAL INFORMATION."

DETERMINATION OF NET ASSET VALUE

The Net Asset Value of the Fund shall be its assets less its liabilities, determined in accordance with United States generally accepted accounting principles ("US GAAP"), except that the Fund may elect to modify the treatment of organizational costs and expenses to accommodate its practical needs, including without limitation, by amortizing such costs and expenses over a period of up to 60 months. The Directors may, in their absolute discretion and where considered to be in the best interests of the

Fund, decide not to follow US GAAP. The Net Asset Value is calculated by the Administrator, on a quarterly basis, subject to the overall supervision of the Directors acting in good faith. The Net Asset Value of the Fund shall be the value of its gross assets less its gross liabilities (excluding accrued Incentive Fees) on any Valuation Date. The Net Asset Value Per Share as of any Valuation Day shall be the net asset value of those assets and liabilities of the Fund which are properly attributable to the Series of Shares of which that Share forms a part, divided by the number of Shares of the Series outstanding on that day.

181 (2)

No. 10-695

In the Supreme Court of the United States

MARK D. LAY, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether, in a prosecution for investment adviser fraud under 15 U.S.C. 80b-6, the jury permissibly found, on the facts of this case, that a hedge fund adviser owed fiduciary duties to the sole investor in his hedge fund.

2. Whether the evidence was sufficient to support petitioner's convictions for mail fraud (18 U.S.C. 1341) and conspiracy to commit mail and wire fraud (18 U.S.C. 1349).

3. Whether, in permitting the rereading to the jury of petitioner's deposition testimony from a civil case, the district court gave an adequate cautionary instruction.

TABLE OF CONTENTS

Page

Opinions below 1
Jurisdiction 1
Statement 2
Argument 8
Conclusion 14

TABLE OF AUTHORITIES

Cases:

Goldstein v. *SEC*, 451 F.3d 873 (D.C. Cir. 2006) ... *passim*
Schmuck v. *United States*, 489 U.S. 705 (1989) 12
Skilling v. *United States*, 130 S. Ct. 2896 (2010) 13
United States v. *Grossman*, 843 F.2d 78 (2d Cir. 1988), cert. denied, 490 U.S. 1059 (1989) 13
United States v. *Marando*, 504 F.2d 126, cert. denied, 419 U.S. 1000 (1974) 13
United States v. *Rodgers*, 109 F.3d 1138 (6th Cir. 1997) 14

Statutes and regulation:

Investment Advisers Act of 1940, ch. 686, Tit. II, 54 Stat. 847 (15 U.S.C. 80b-1 *et seq.*) 4
15 U.S.C. 80b-2(a)(11) 9
15 U.S.C. 80b-3(b)(3) 8, 10
15 U.S.C. 80b-6 ..... 2, 3, 4, 10
15 U.S.C. 80b-6(1)-(2) 4
15 U.S.C. 80b-6(4) 5, 11
15 U.S.C. 80b-17 3

Statutes and regulation—Continued: Page

18 U.S.C. 2 ..... 2, 4
18 U.S.C. 1341 ..... 2, 3, 13
18 U.S.C. 1343 3
18 U.S.C. 1346 14
18 U.S.C. 1349 ..... 2, 3
17 C.F.R. 275.206(4)-8 11

Miscellaneous:

SEC, *Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles*, Release No. IA-2628 (Aug. 3, 2007), http://www.sec.gov/rules/final/2007/ia-2628.pdf 11

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. B1-B27) is reported at 612 F.3d 440. The opinion of the district court denying petitioner's motion for acquittal or for a new trial is reported at 566 F. Supp. 2d 652.

JURISDICTION

The judgment of the court of appeals was entered on July 14, 2010. A petition for rehearing was denied on August 25, 2010 (Pet. App. A1-A2). The petition for a writ of certiorari was filed on November 23, 2010. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

Following a jury trial in the United States District Court for the Northern District of Ohio, petitioner was convicted of one count of investment adviser fraud, in violation of 15 U.S.C. 80b-6; one count of conspiracy to commit or attempt mail and wire fraud, in violation of 18 U.S.C. 1349; and two counts of mail fraud, in violation of 18 U.S.C. 1341 and 2. Pet. App. C2. He was sentenced to 144 months of imprisonment, to be followed by three years of supervised release. *Id.* at C4-C5. He was also ordered to forfeit $590,526 and to pay $212,967,084 in restitution. *Id.* at C9. The court of appeals affirmed. *Id.* at B1-B27.

1. Petitioner was the chairman of an investment advisory firm that was hired in the 1990s by the Ohio Bureau of Workers' Compensation (Bureau), a state agency that assists employers with expenses related to workplace injuries. *United States* v. *Lay*, 566 F. Supp. 2d 652, 655-656 (N.D. Ohio 2008). The firm was initially retained to manage the Bureau's investment in a long-term bond fund known as the "Long Fund." *Id.* at 656.

Petitioner later founded the "Active Duration Fund," a hedge fund that consisted primarily of government, corporate, and mortgage-backed securities. *Lay*, 566 F. Supp. 2d at 656. In 2003, he successfully solicited the Bureau to transfer $100 million from the Long Fund to the Active Duration Fund. *Id.* at 657. The Bureau believed that the Active Duration Fund was "very conservative" and "low risk," and it intended its investment in that fund as a "hedge" that would "diversify[]" its Long Fund investment. Pet. App. B6. During the relevant time period, the Bureau was the Active Duration Fund's

sole investor and paid petitioner's firm nearly $2 million in fees for services related to that investment. *Lay*, 566 F. Supp. 2d at 656-657.

The agreement governing the Active Duration Fund set a non-binding "leveraging guideline"—a guideline reflecting the extent to which the fund would take financial positions, through borrowing or otherwise, in excess of its actual assets—of 150%. Pet. App. B3, D13. In practice, petitioner routinely leveraged fund assets much more than that: two-thirds of the trades involved leveraging over 150%; over one-fifth involved leveraging over 1000%; and some trades involved leveraging over 10,000%. *Id.* at B3, B13. Petitioner concealed and misrepresented to the Bureau his true leveraging practices, the magnitude of losses that the fund began to experience, and the magnification of losses caused by his leveraging beyond 150%. *Lay*, 566 F. Supp. 2d at 657.

In 2004, the Bureau, believing that the Active Duration Fund had lost only $7 million when in fact it had lost $32 million, transferred another $100 million to that fund from the Long Fund. Pet. App. B3-B4; *Lay*, 566 F. Supp. 2d at 657. Later that year, the Bureau discovered petitioner's leveraging practices; it invested another $25 million in an attempt to avoid a complete loss of the $200 million it had already invested. Pet. App. B3; *Lay*, 566 F. Supp. 2d at 658. It ultimately recovered only $9 million of the total $225 million. Pet. App. B4.

2. A grand jury returned a superseding indictment charging petitioner with one count of investment adviser fraud, in violation of 15 U.S.C. 80b-6 and 80b-17; one count of conspiracy to commit or attempt mail and wire fraud, in violation of 18 U.S.C. 1341, 1343, and 1349; and two counts of mail fraud, in violation of 18 U.S.C. 1341

and 2. *Lay*, 566 F. Supp. 2d at 679-689. The mail fraud charges (and, in part, the conspiracy charge) were based on "Trade Confirmation Statements," which documented fund transactions, that petitioner had mailed to the Bureau. *Id.* at 686-687.

Section 80b-6, which is part of the Investment Advisers Act of 1940, ch. 686, Tit. II, 54 Stat. 847 (15 U.S.C. 80b-1 *et seq.*), makes it unlawful for an "investment adviser" to use the mails or the instrumentalities of interstate commerce:

> (1) to employ any device, scheme, or artifice to defraud any client or prospective client;
>
> (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client;
>
> * * * * *
>
> (4) to engage in any act, practice or course of business which is fraudulent, deceptive, or manipulative. The Commission shall, for the purposes of this paragraph (4) by rules and regulations define, and prescribe means reasonably designed to prevent, such acts, practices, and courses of business as are fraudulent, deceptive, or manipulative.

15 U.S.C. 80b-6(1)-(2) and (4). At trial, over petitioner's objection, the district court instructed the jury that, assuming it found petitioner had committed a fraud, such fraud would violate Section 80b-6 if the jury found either that (a) the Bureau was petitioner's "client" with respect to the Active Duration Fund, see 15 U.S.C. 80b-6(1)-(2); or (b) that petitioner owed the Bureau a

fiduciary duty with respect to that fund, see 15 U.S.C. 80b-6(4). Pet. App. B9-B11.

During deliberations, the jury asked to rehear deposition testimony that petitioner had given in a previous civil case, which had been admitted into evidence over petitioner's objection. Pet. App. B20-B22. In that deposition, petitioner had repeatedly stated that the Bureau was his "client" with respect to the Bureau's investment in the Active Duration Fund. *Id.* at B21. The district court permitted the deposition to be reread in its entirety, but cautioned the jury "not to accord undue influence to that testimony." *Lay*, 566 F. Supp. 2d at 678; Pet. App. B21.

The jury found petitioner guilty on all four counts. Pet. App. B11. It also found, on a special verdict form, that petitioner obtained $590,526 in proceeds from his offenses. *Ibid.*

3. Petitioner moved for acquittal or for a new trial. The district court denied the motion. *Lay*, 566 F. Supp. 2d at 652.

Petitioner's primary argument was that, as a matter of law, he had neither a client relationship with, nor a fiduciary duty to, the Bureau with respect to the Active Duration Fund. *Lay*, 566 F. Supp. 2d at 668-671. Relying on *Goldstein* v. *SEC*, 451 F.3d 873 (D.C. Cir. 2006), petitioner asserted that he was the adviser to the fund itself, not the adviser to the Bureau. *Lay*, 566 F. Supp. 2d 668-671. The district court rejected petitioner's reading of *Goldstein*. It observed that although *Goldstein* had found the "characteristics defining an adviser-client relationship * * * to ordinarily be absent in hedge fund scenarios," in petitioner's particular case, "there is evidence in the record that the characteristics of an

adviser-client relationship were present." *Id.* at 670. In reaching that record-based conclusion, the district court focused on petitioner's preexisting fiduciary relationship with the Bureau regarding the Long Fund; evidence that the Bureau was the sole shareholder in the Active Duration Fund; evidence that the purpose of the Active Duration Fund was to provide a hedge for the Bureau's Long Fund investment, which petitioner managed; and evidence of petitioner's "regular and direct communication" with the Bureau about his management of the Active Duration Fund. *Id.* at 670-671.

Petitioner raised a number of additional arguments, all of which the district court rejected. In particular, the district court rejected, based on the evidence, petitioner's assertion that there was "no evidence that the mails were used to exceed * * * the leverage guidelines." *Lay*, 566 F. Supp. 2d at 671 n.56. The district court also held that the limiting instruction it had given in connection with the rereading of petitioner's deposition had been sufficient. *Id.* at 677-678.

4. The court of appeals affirmed. Pet. App. B1-B27. It agreed with the district court that it was permissible, and consistent with *Goldstein*, for the jury to "determine the existence of a fiduciary relationship * * * on the facts of this case." *Id.* at B17. It explained that "*Goldstein* did not hold that *no* hedge fund adviser could create a client relationship with an investor, but rather held only that the SEC had 'not justified treating *all* investors in hedge funds as clients.'" *Ibid.* (quoting *Goldstein*, 451 F.3d at 883) (first emphasis added). The court of appeals concluded, essentially for the reasons stated by the district court, that "the relationship between the Bureau and [petitioner] as to the Active Dura-

tion Fund was not a typical hedge fund adviser-investor relationship" and that a finding of a fiduciary duty was supported by the evidence. *Id.* at B17-B18; see *id.* at B14-B15.

Petitioner raised several additional arguments, all of which the court of appeals rejected. Petitioner asserted that the 150% leverage limit for the fund "served only as a guideline rather than a binding limitation," but the court concluded that the contemplated leeway did "not permit leveraging over 150% in two-thirds of trades and leveraging over 1000% in one-fifth of trades." Pet. App. B18. Petitioner also argued that insufficient evidence supported the mail- and wire-fraud-related convictions, but the district court concluded (among other things) that the "trade confirmations, emails, and faxes through which [petitioner] conducted the fraud satisfy the mailing and wiring requirements because these documents were designed to lull the victims into a false sense of security, postpone their ultimate complaint to the authorities, and therefore make the apprehension of the defendants less likely than if no mailings had taken place." *Id.* at B19 (internal quotation marks and citation omitted). And petitioner additionally argued that the district court should have instructed the jury, when his deposition testimony was reread, not to take the testimony out of context; the court of appeals concluded that such an instruction was unnecessary because "the entirety of [petitioner's] deposition testimony was re-read to the jury." *Id.* at B21.

Judge Kethledge concurred in part and dissented in part. Pet. App. B24-B27. He disagreed with the majority's conclusion that sufficient evidence supported the mail-fraud convictions; in his view, the trade confirma-

tion slips that petitioner mailed to the Bureau "were too remote from the antecedent fraud, and too speculative in their effects, to support a finding that they were designed to lull the victims into a false sense of security." *Id.* at B26 (internal quotation marks and citation omitted). Judge Kethledge recognized, however, that "even under [his] proposed disposition of this case, [petitioner's] sentence would remain the same." *Ibid.*

ARGUMENT

1. Petitioner first contends (Pet. 14-35) that the court of appeals' decision in this case conflicts with the D.C. Circuit's decision in *Goldstein* v. *SEC*, 451 F.3d 873 (2006). According to petitioner, *Goldstein* holds that, as a matter of law, a hedge-fund adviser can never have a client relationship or other fiduciary relationship with a hedge fund investor. As both lower courts correctly concluded, petitioner misreads *Goldstein*.

In *Goldstein*, the D.C. Circuit invalidated a Securities and Exchange Commission (SEC) regulation interpreting a section of the Investment Advisers Act of 1940 (Act) not directly at issue here, 15 U.S.C. 80b-3(b)(3), which exempts advisers with fewer than 15 "clients" from the requirement to register with the SEC. See 451 F.3d at 877, 884. The regulation had interpreted the term "client" in such a way that investors in hedge funds would generally be considered "clients" of a hedge fund adviser. *Id.* at 877.

The D.C. Circuit held that the SEC had "not adequately explained how the relationship between hedge fund investors and advisers justifies treating the former as clients of the latter." *Goldstein*, 451 F.3d at 882. The court observed that while the term "client" was not de-

fined in the Act, the term drew meaning from the definition of "investment adviser," which is defined as "any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities." 15 U.S.C. 80b-2(a)(11); see *Goldstein*, 451 F.3d at 879. The D.C. Circuit stated that in hedge funds, an investor does not receive direct advice from an adviser about how to spend his money; instead, the investor purchases a share of the fund and allows its money to be controlled by the hedge fund adviser. *Ibid.* According to the court, the adviser "owes fiduciary duties only to the fund, not to the fund's investors" and "the adviser [would] inevitably face conflicts of interest" if fiduciary duties were owed to both. *Id.* at 881.

The D.C. Circuit did not, however, foreclose the possibility that a client or fiduciary relationship might exist in special cases, different from the general hedge fund operations it had described. The SEC pointed out that "a hedge fund adviser may not treat all of its hedge fund investors the same"; the court responded, in part, by stating that "[i]f there are certain characteristics present in some investor-adviser relationships that mark a 'client' relationship, then the [SEC] should have identified those characteristics and tailored the rule accordingly." *Goldstein*, 451 F.3d at 882-883. The rule the SEC had promulgated, however, "ha[d] not justified treating *all* investors in hedge funds as clients." *Id.* at 883; see *ibid.* (criticizing SEC for "painting with such a broad brush").

Goldstein accordingly leaves open the possibility that a narrower regulation, defining only some hedge fund

investors as "clients" within the meaning of 15 U.S.C. 80b-3(b)(3), might be permissible. It necessarily follows that *Goldstein* does not preclude the possibility that, in a prosecution under a separate section of the Investment Advisers Act, 15 U.S.C. 80b-6, a jury might conclude that a client or fiduciary relationship existed on a particular fact pattern. In particular, *Goldstein* is silent on whether a fiduciary relationship could arise on facts like those in this case, which, as the court of appeals recognized, lie far afield from the generic hedge fund scenario contemplated in *Goldstein*.[1]

As the court of appeals concluded (Pet. App. B17-B18), unlike a typical hedge fund adviser, petitioner had an individualized, person-to-person relationship with the Bureau concerning its investment in the Active Duration Fund. Petitioner "has never disputed" his preexisting fiduciary relationship with the Bureau with respect to the Long Fund, and "evidence supports the conclusion that this relationship continued through the existence of the Active Duration Fund and encompassed the Bureau's Active Duration Fund investment," which was designed as a hedge for the Long Fund investment. Pet. App. B14. "Unlike a typical hedge fund investor," the Bureau played "an active role" in its investment. *Id.* at B15; cf. *Goldstein*, 451 F.3d at 880 (describing scenario where investor "fades into the background" once the investment is made). Also "[u]nlike a typical hedge fund investor, the Bureau was the only investor in the Active

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[1] Petitioner raises (*e.g.*, Pet. 21-22, 29-34) a number of challenges to the jury's conclusion that a client or fiduciary relationship existed on this case. Those fact-bound arguments do not merit this Court's review.

Duration Fund at the relevant time," Pet. App. B15, eliminating the possibility of the sort of conflicts of interest that troubled the D.C. Circuit in *Goldstein*, see 451 F.3d at 881.

c. Further regulatory developments also render certiorari, based on petitioner's claim of tension between *Goldstein* and the result in this case, unwarranted. Shortly after *Goldstein*, the SEC promulgated a new rule clarifying that Section 80b-6(4) prohibits investment advisers from defrauding investors or prospective investors in pooled investment vehicles, including hedge funds, without regard to whether a fiduciary relationship exists. 17 C.F.R. 275.206(4)-8; see SEC, *Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles*, Release No. IA-2628, at 4-5 (Aug. 3, 2007) (SEC Rule) (intention of rule "is to prohibit all fraud on investors in pools managed by investment advisers" and rule applies to hedge fund advisers), http://www.sec.gov/rules/final/2007/ia-2628.pdf.[2] Because the new rule prospectively resolves the issue of whether an adviser's fraud on a hedge fund investor is criminalized by the Investment Advisers Act, the question presented has limited future importance.

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[2] Petitioner argues (Pet. 25) that the new rule *supports* review here, because the rule "does not create under the Advisers Act a fiduciary duty to investors or prospective investors in a pooled investment vehicle not otherwise imposed by law." SEC Rule 13. Petitioner misunderstands the import of the rule. Under the new rule, it *does not matter* whether a hedge fund adviser owes fiduciary duties to a hedge fund investor; defrauding such an investor will be illegal regardless. *Id.* at 14; see 17 C.F.R. 275.206(4)-8; see also 15 U.S.C. 80b-6(4) (permitting SEC to define investment adviser frauds without regard to whether they are committed against a "client").

2. Petitioner also raises challenges to the sufficiency of the evidence on his mail-fraud and conspiracy convictions. Pet. 35-48. These largely fact-bound challenges lack merit.

Petitioner first asserts (Pet. 36-37, 41) that there "was no evidence * * * that the [Bureau] parted with property by reason of a material misrepresentation." That assertion was rejected by the courts below. See Pet. App. B18-19 (petitioner's "misrepresentations of his leveraging activity caused the Bureau to part with money"); *Lay*, 566 F. Supp. 2d at 671 n.56 ("There is evidence in the record that the [Bureau] would not have transferred funds to the [Active Duration Fund] if aware of over-leveraging."). No further review is warranted.

Petitioner next challenges his mail-fraud convictions on the ground that the only mailings mentioned in the indictment—the trade confirmation statements—did not contain false information and were not themselves used to obtain the Bureau's property. Pet. 37-42. As this Court has made clear, however, "the use of the mails need not be an essential element of the scheme" in a mail-fraud prosecution, *Schmuck* v. *United States*, 489 U.S. 705, 710 (1989), and "routine mailings that are innocent in themselves" can supply the mailing element so long as they are "incident to an essential part of the scheme, or a step in the plot." *Id.* at 710-711, 714-715 (internal quotation marks, citation, and brackets omitted); see *id.* at 712 (mailing of title-registration forms in odometer-tampering scheme was necessary to passage of title and thus to the scheme, even though they "may not have contributed directly to the duping of either the retail dealers or the customers"). Here, the mailing of the confirmation statements was necessary to the settle-

ment of the fund's trades, see Gov't C.A. Br. 51-52, and, as the court of appeals found, they served to lull the Bureau into a false sense of security and thereby postpone discovery of the fraud. Pet. App. B19. The Second Circuit cases cited by petitioner (Pet. 38) are consistent with that conclusion. See *United States* v. *Grossman*, 843 F.2d 78, 86 (1988) (confirmation slips furthered scheme in part because they "concealed the fraud by maintaining an appearance of normality"), cert. denied, 490 U.S. 1059 (1989); *United States* v. *Marando*, 504 F.2d 126, 130 (confirmation slips "ostensibly legitimatized the fraud and provided it with the appearance of normality"), cert. denied, 419 U.S. 1000 (1974).

Petitioner finally contends (Pet. 42-48) that the court of appeals' decision conflicts with this Court's decision in *Skilling* v. *United States*, 130 S. Ct. 2896 (2010). That contention lacks merit. *Skilling* did not address the definition of money or property fraud under the mail-fraud statute at issue here (18 U.S.C. 1341), but instead interpreted 18 U.S.C. 1346's prohibition against "honest services" mail or wire fraud. In explaining the historical development of the honest services doctrine, the Court noted that unlike traditional fraud cases—in which "the victim's loss of money or property supplied the defendant's gain, with one the mirror image of the other"—the defrauded party in an honest services scheme suffered no money or property deprivation. 130 S. Ct. at 2926. That observation has no bearing on this case. Notwithstanding petitioner's assertion to the contrary (*e.g.*, Pet. 43), he did in fact gain at the Bureau's expense: while the Bureau paid nearly $2 million in fees, the jury specifically found (and the court of appeals affirmed) that petitioner "obtained $590,526.23 in pro-

ceeds from his mail and wire fraud offenses." Pet. App. B11; *Lay*, 566 F. Supp. 2d at 654, 656-657.

3. Petitioner finally contends (Pet. 48-49) that a new trial is warranted because the district court declined to instruct the jury not to take his deposition testimony out of context when it was reread during deliberations. Petitioner fails to explain why it was necessary to give such an instruction when "the *entirety* of [petitioner's] deposition testimony was re-read to the jury." Pet. App. B21 (emphasis added); see *United States* v. *Rodgers*, 109 F.3d 1138, 1143 (6th Cir. 1997) (where jury heard the entire testimony of a witness, it could not have taken part of it out of context). He furthermore fails to assert that any other court of appeals would have required such an instruction. Further review is unwarranted.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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JANUARY 2011

Supreme Court, U.S.
FILED
FEB 8 - 2011
OFFICE OF THE CLERK

Nº. 10-695

In The
Supreme Court of the United States

MARK D. LAY,
Petitioner,
v.
UNITED STATES OF AMERICA,
Respondent.

Petition For A Writ Of Certiorari To The United States Court of Appeals For The Sixth Circuit

REPLY BRIEF OF PETITIONER MARK D. LAY

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TABLE OF CONTENTS

Table of Contents i

Table of Authorities ii

Reply Brief 1

Argument 3

Conclusion 21

TABLE OF AUTHORITIES

Cases

Cleveland v. United States,
531 U.S. 12 (2000) 16

Pereira v. United States,
346 U.S. 1, 98 L. Ed. 435, 74 S. Ct. 358 (1954) . . . 16

United States v. Cohen,
518 F.2d 727, 737 (2 Cir) 16

United States v. Grossman,
843 F. 2d 78 (2d Cir. 1988) 16, 17

United States v. Males,
459 F. 3d 154 (2d Cir. 2006) 17

United States v. Marando, 504 F.2d 126(2d) . . . 15

United States v. Maze, 414 U.S. 395 (1974) 16

United States v. Smith,
419 F. 3d 521 (6th Cir. 2005) 2, 19, 20

United States v. Tines,
70 F.3d 891, 897 (6th Cir. 1995) 19

Statutes

15 U.S.C. §80b-2(11) 6

15 U.S.C. §80b-3(b)(2) 2

18 U.S.C. §1341 . . . . . 15, 16, 18

Other Authorities

Investment Advisers Act of 1940,
Release No. IA-3110
(November 19, 2010) 3

Proposed Rule: Exemptions for Advisers
to Venture Capital Funds, Private
Fund Advisers, Release No. IA-3111
(November 19, 2010) 4

REPLY BRIEF OF PETITIONER MARK D. LAY

The Opposition of the United States is gravely flawed in the following numerous respects, evincing a need for further review of the Court of Appeals opinion affirming Petitioner's conviction:

1. Contrary to the Opposition claim,the Ohio Bureau of Workers Compensation (OBWC) did not pay Petitioner $2.million in fees for services related to the Active Duration Fund (ADF). As the express terms of the relevant Private Placement Memorandum (PPM) provide, all fees were paid by ADF, through the ADF Administrator, Olympia Capital.OBWC did not pay any fees to Petitioner for ADF.

2. Given the formula under which the fees of the ADF Investment Adviser, Petitioner, were calculated, it would have been impossible for OBWC to determine how much Petitioner was due in fees without knowing the net asset value of ADF. Accordingly, contrary to the Opposition argument, Petitioner could not have concealed and misrepresented the magnitude of leverage or losses, given that knowledge of these matters is an essential component to computing what amount of fees were owed.

3. Contrary to the Opposition argument, the opinion of the District of Columbia Court of Appeals in Goldstein indeed held that no hedge fund adviser could create a client relationship with a hedge fund investor and did not leave open the possibility that a narrower regulation than the proposed SEC Rule might be permissible under 15 U.S.C. §80b-3(b)(2).

4. Contrary to the Opposition argument, SEC Rule 13 merely criminalized certain hedge fund adviser conduct, it did not overrule Goldstein.

5. The Opposition merely parrots the unsupported statement in the Court of Appeals opinion that trade confirmation slips lulled OBWC into a sense of security. There was no evidence of any nature to support the requirement that these slips in some manner caused OBWC to part with money or property; and

6. The Court of Appeals failed to follow its own decision in United States v. Smith, 419 F. 3d 521 (6th Cir. 2005) concerning the limiting instructions that should have been given to the jury in connection with the reading of Petitioner's civil deposition testimony.

These weaknesses in the Opposition combine with the novel nature of the investor/client conflicting circuit court opinions to render the need for further appellate review here essential.

Accordingly, it is respectfully requested that certiorari be granted.

ARGUMENT

The Opposition of the United States underscores the need for further review of the Opinion of the Court of Appeals for the reason it fails to address the ongoing regulatory measures being taken by the Securities and Exchange Commission to clarify duties owed by investment advisers to private funds, such as the Active Duration Fund here.[1] The Opposition also would

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1 The SEC has now proposed rules to implement certain provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act regarding investment advisers to private funds, such as hedge funds and private equity funds...

Proposed Rule: Rules Implementing Amendments to the Investment Advisers Act of 1940, Release No. IA-3110 (November 19, 2010), available at http://sec.gov/rules/proposed/201/ia-3110.pdf (the "implementing release"); and Proposed Rule:

have this Court totally ignore all of the operative agreements that governed ADF, Petitioner's relationship to OBWC, and the limitation imposed by these agreements, including the restrictions of hedge fund investments to qualified or sophisticated investors.

The Opposition incorrectly states that Petitioner received compensation from the Ohio Bureau of Workers Compensation (OBWC) for services as the ADF Investment Adviser. The express terms of the governing agreements, i.e. the PPM and ADF investment adviser agreement refute this. Furthermore, there was no evidence whatsoever in the form of checks or transfers of any nature to establish that any fees paid to Petitioner were paid by OBWC, all fees having instead been paid, in accordance with the ADF Private Placement Memorandum by the Fund Administrator, Olympia Capital. The Opposition attempts to create an investment structure that is a

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Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers, Release No. IA-3111 (November 19, 2010), available at http://www.sec.gov/rules/proposed/2010/ia-3111.pdf (the "exemptions release"). (See, Sullivan & Cromwell, LLP, November 24, 2010 Newsletter)

attempts to create an investment structure that is a complete fiction. It ignores both the fundamental agreements governing ADF and its operation, and the motivation of an investor such as OBWC to invest in a hedge fund, which is the opportunity to realize more lucrative returns from exotic investments and riskier investments that are unavailable to the general investing public.

The inconsistent arguments advanced by the United States support the need for further review. There is no other case known to Petitioner where it has been determined that a hedge fund investor may also be a hedge fund client.

Under Goldstein it is clear that investment advisers do not owe fiduciary duties to hedge fund investors for the reason the investors are not the advisers' clients and as such observing fiduciary duties to the investor instead of the fund would pose inevitably conflicts of interests.

In point of fact, Goldstein states:

> [C]ongress did not intend "shareholders, limited partners, members, or beneficiaries" of a hedge fund to be counted as "clients." Although the statute does not define "client," it does define "investment

adviser" as "any person who, for compensation, engages in the business of advising others, either *directly* or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities." *15 U.S.C. §80b-2(11)* [**19] (emphasis added). An investor in a private fund may benefit from the adviser's advice (or he may suffer from it) but he does not receive the advice *directly*. He invests a portion of his assets in the fund. The fund manager - the adviser - controls the disposition of the pool of capital in the [*880] fund. The adviser does not tell the *investor* how to spend his money; the investor made that decision when he invested in the fund. Having bought into the fund, the investor fades into the background; his role is completely passive. If the person or entity controlling the fund is not an "investment adviser" to each individual investor, then *a fortiori* each investor cannot be a "client" of that person or entity. These are just two sides of the same coin...

> If the investors are owed a fiduciary duty and the entity is also owed a fiduciary duty, then the advisor will inevitably face conflicts of interest. Consider an investment adviser to a hedge fund that is about to go bankrupt. His advice to an investor in the fund, however, would likely include any and all measures to remain solvent. [**25] His advice to an investor in the fund, however, would likely be to sell. For the same reason, we do not ordinarily deem them the shareholders in a corporation the "clients" of the corporation's lawyer or accountants. *See RESTATEMENT, supra §96 cmt. B* ("By representing the organization, a lawyer does not thereby also form a client-lawyer relationship with all or any individuals...who have an ownership or other beneficial interest in it, such as its shareholders"). While the shareholders may benefit from the professionals' counsel indirectly, their individual interest easily can be drawn into conflict with the interest of the entity. It simply cannot be the case that investment advisers are the servants of two masters in this way.

Id. (Emphasis added.)

In light of the language it is erroneous to state Goldstein left the issue open.

In May of 2002, MDL founded the exempt ADF Hedge Fund in Bermuda. **Due to the nature of this investment vehicle and the rules and regulations related hereto, the ADF Hedge Fund was required to be established pursuant to a completely separate and distinct business relationship between MDL and the Bureau that was not connected to and in way dependent upon the pre-existing relationship with the Bureau**. (Emphasis added). The ADF Hedge Fund consisted primarily of government, corporate, and mortgage-backed securities.

The ADF Hedge Fund was intended to receive the investments of the Bureau and potentially other investors as well. (Testimony of T.C. Gasper, Doc. #102, p. 43). In bond markets, long term bonds generally decline in value in a rising interest rate environment. Thus a fund that allows an investor to maximize its short bond position is a natural "hedge" against rising interest rates. Short selling, or leveraging, increases the advantage of taking a short position in the bond market. The primary document governing the creation of the ADF Hedge Fund and the business

relationship the Bureau, Lay and MDL was the Private Placement Memorandum (hereinafter referred to as the "PPM."). In the PPM, the ADF Hedge Fund was part of an overlay strategy to assist in protecting the Bureau's overall portfolio of investments from the threat of rising interest rates: "The Fund will seek to capture significant gains during periods when interest rates are generally declining and will seek to protect principal during periods when rates are generally increasing." (PPM, p.iv).

It is common knowledge now and at the time this fund was created that a hedge fund is a high risk investment vehicle.

Several specific examples of this exist in the PPM. At the outset of the PPM, it is stated, in all capital letters:

> PROSPECTIVE SUBSCRIBERS IN THE FUND SHOULD INFORM THEMSELVES AS TO THE LEGAL REQUIREMENTS AND TAX CONSEQUENCES WITHIN THE COUNTRIES OF THEIR RESIDENCE AND DOMICILE FOR THE ACQUISITION, HOLDING OR DISPOSAL OF SHARES AND ANY FOREIGN EXCHANGE REGISTRATIONS WHICH MAY BE RELEVANT TO THEM. IF YOU ARE IN ANY

> CONSULT YOUR STOCKBROKER, SOLICITOR, ACCOUNTANT OR OTHER FINANCIAL ADVISER.

(PPM, p. ii).

(PPM, p. 23). (emphasis in the original).

Investors are further informed that, due to the nature of ADF Hedge Finds, they are not afforded the same protections as more conservative investment vehicles...

> THE PURCHASE OF SHARES IS SPECULATIVE AND INVOLVES A HIGH DEGREE OF RISK. THERE IS NO ASSURANCE THAT THE FUND WILL BE PROFITABLE. SEE THE SECTION ENTITLED "RISK FACTORS" WITHIN THIS MEMORANDUM FOR A DESCRIPTION OF CERTAIN RISKS INVOLVED IN THE PURCHASE OF SHARES.

(PPM, p. iii) (Emphasis in the original).

The following excerpts from the PPM totally refute the Opposition claim that OBWC paid Petitioner's fees:

Investment Adviser Compensation

The Investment Adviser will receive a quarterly management fee determined at a rate equal to 1% per annum of the Fund's Net Asset Value, accrued monthly and payable in arrears as of the end of each calendar quarter. It also will receive a quarterly inventive fee (the "Incentive Fee") equal, in the aggregate, to 20% of the increase in Net Asset Value of each series of Shares over the sum of (i) the Series' Net Asset Value as of the commencement of each calendar quarter plus (ii) the yield on the Fund's portfolio at a rate equal to the yield of the Lehman Government Credit Index for such period (the "Hurdle"). A series of Shares will only be charged with an Incentive Fee if its Net Asset Value at the end of a quarter (prior to accrued Incentive Fees), if any, for the quarter is greater that (i) its Net Asset Value at the time of its initial subscription (or the Initial Closing Date, whichever is later) or (ii) its Net Asset Value at the time the last Incentive Fee was charged against such Series, whichever is higher, plus the Hurdle (the "High Water Mark"). In the event that the

Fund invests in the Master Fund, the Investment Adviser will not be entitled to a separate management or investment advisory fee as manager of the Master Fund but will be entitled to reimbursement for expenses incurred on behalf of the Master Fund...

Calculation of Investment Adviser Compensation

The Fund will pay a management fee to the Investment Adviser equal to 1% per annum of the Fund's Net Asset Value at the end of each calendar quarter. The management fee is accrued monthly in arrears and paid as of the end of each calendar quarter.

The Fund also will pay a quarterly Incentive Fee to the Investment Adviser equal to 20% of "Net Profit" with respect to each series of Shares. See "SERIES OF SHARES" below. "Net Profit" is defined as the excess of the Net Asset Value of a Series as of the end of the quarter (after deduction of the Management Fee accrued for the quarter but excluding any deduction for Incentive Fees accrued on each Series) less the sum of (i) the Net Asset

Value of the Series as of the first day of the quarter plus (ii) the amount of interest which would have been earned during the quarter if the Fund's net assets had been invested at a rate equal to the yield on the Lehman Government Credit Index for the quarter (the "Hurdle") adjusted to reflect subscription and redemptions with respect to such period.

Incentive Fees are based only on the portion of the appreciation in the Net Asset Value of a Series of Shares during a quarter that constitutes an increase in its Net Asset Value in excess of the sum of the cumulative Hurdle and its highest Net Asset Value as of the end of any prior quarter or, for the quarter the Series are redeemed at any time other than the end of a quarter, the date of redemption will be treated as such shares. The amount of any Incentive Fee accrued with respect to the redeemed Shares will be payable to the Investment Adviser, notwithstanding that following the redemption, the Net Asset Value of the relevant Series of Shares decreases...

This language in the PPM makes it clear the Petition's fees were paid by Olympia Capital as Administrator for ADF, not OBWC. It also makes clear that whoever paid the fees had to have intimate knowledge of ADF's performance. Accordingly, it is inconsistent to contend, as the Opposition does, that OBWC paid the fees but was misled concerning ADF status. In other words, it is illogical to contend that OBWC paid Petitioner's fees, but was not aware of factors such as the daily net asset value of ADF, a critical component of fee calculation.

OBWC was a sophisticated investor. Participation in ADF was limited to sophisticated investor.

In point of fact the PPM states:

> **Eligible Subscribers**
> The Shares are offered only to Qualified Holders. Qualified Holders are "non-United States Persons" and U.S. tax-exempt investors who are "qualified eligible participants" under CFTC Regulation 4.7 and "qualified purchasers" under Section 3(c)(7) of the Investment Company Act.

The dissent in this action determined that the government's explanation of the significance of mailing trade confirmation slips is amorphous at best. In Petitioner's case all trades were done correctly. The government alleged that the trade confirmations were used in a scheme to over leverage the Active Duration Hedge Fund (ADF). The evidence at trial however did not show how any of the trades accomplished over leveraging. The fact is many trades reduced leverage, and many trades were profitable. The evidence did not address individual trades or the dates of the trades. Without showing the daily position of the fund and any losses generated by the trades, the confirmation slips in and of themselves did not advance the government's case.

The trade confirmation statements did not contain false information. In cases where mailing trade confirmation statements constituted a violation of 18 U.S.C. §1341, the statements were transmitted for the purposes of executing the artifice of scheme. See, United States v. Marando, 504 F.2d 126(2d Cir. 1974) where trade confirmation slips were mailed and determined to be an integral part of a scheme to obtain property; also see,

United States v. Grossman, 843 F. 2d 78 (2d Cir. 1988) where it was determined that:

> The mailings of the confirmation slips did further the purpose of executing the scheme. The confirmation slips (1) notified the relatives that the purchase or sale actually had been completed; (2) provided an on-going tally of purchases, allowing the relatives to cover each other's positions; (3) concealed the fraud by maintaining an appearance of normality, see, United States v. Cohen, 518 F.2d 727, 737 (2 Cir), cert denied, 423 U.S. 926, 46 L. Ed. 2d 252 (1975): and (4) allowed the relatives to demonstrate ownership after the recapitalization announcement. Pereira v. United States, 346 U.S. 1, 98 L. Ed. 435, 74 S. Ct. 358 (1954). [**27].

To establish a violation of the mail fraud statute, "the mailing must be for the purposes of executing the scheme." United States v. Maze, 414 U.S. 395 (1974). To state an offense under 18 U.S.C. §1341 this Court determined in Cleveland v. United States, 531 U.S. 12 (2000) that the evidence must show that the defendant not only devised scheme or artifice, but also used that scheme or artifice to

obtain money or property. See, United States v. Males, 459 F. 3d 154 (2d Cir. 2006) (Emphasis added). Here the evidence showed ADF received its first $100,000,000.00 before Mr. Lay ever executed a trade. There was no evidence that the mail was used to obtain money or property. There was no evidence that property or money was obtained through a scheme that involved the use of the mail. The trade confirmation slips here unlike those in Grossman or Mirando did not contain false information, did not document illegal insider trades, and were not transmitted to obtain money or property. The alleged nondisclosures and misrepresentations concerning leverage alleged by the government were not related to the mailing of confirmation slips. The trades reflected on the listed slips were lawful trades for a hedge fund. It does not matter that OBWC did not authorize them, the relevant private placement memorandum gave ADF's board sole discretion to deviate from the fund's leverage guideline, not OBWC. The trade confirmation statements report the purchases of securities on a certain date, from a certain broker, at a certain price. All of that information was true, in every instance. On these

facts a violation of 18 U.S.C. §1341 was not established.

Here OBWC invested funds in ADF on three discrete dates, August 20, 2003, May 21, 2004 and September 23, 2004. These are the only times OBWC "parted" with property.

In Skilling the Court pointed out the requirement for symmetry in a standard mail fraud case, that is the victim's loss of money or property supplied the defendant's gain with one the mirror image of the other. Id. at *82. Here there was no gain to Petitioner.

The District Court stated in Petitioner's sentencing memorandum:

> Looking back in hindsight, as the Court can do, it seems obvious that he should have stopped following the investment strategy he had in place. But at the time, no one had ever seen an instance in which rising bond process would not lead to a devaluation of existing bonds. But that is precisely what happened in this time frame. It was the first time in economic history of the United States that that occurred, and his strategy

> failed and because of the leverage, failed dramatically.
>
> ***
>
> It seems apparent that the defendant had not lost any monies for any clients in the management of the MDL investments until the defendant began excessive over-leveraging with the ADF... It does not appear to the Court that the defendant was motivated to gain more income by his management of the ADF.

(Trial Court Doc. #181 p. 23) (emphasis added).

Aside from errors related to fees, status as a client, the lack of gain and fraudulent mailings, the District Court erroneously failed to issue a proper limiting instruction as required by United States v. Smith, 419 F.3d 521, 529 (6th Cir. 2005). Therein, the Sixth circuit stated that it is an abuse of discretion to fail to give a proper cautionary instruction "'to guard against the dangers of undue emphasis and context.'" Id. (quoting, United States v. Tines, 70 F.3d 891, 897 (6th Cir 1995). Smith emphasized the need to instruct as to both components, to prevent the undue influence on the jury regarding the testimony and to prevent taking the testimony out

of context of the circumstances of the original testimony. Id.

During the jury deliberations, the jury requested to see the transcript of Petitioner's prior testimony. Prior to allowing the jury's request, and over Petitioner's objections, Judge Dowd of the District Court stated that he was only giving half of the instruction required by the Smith case because he did not understand the second requirement to caution the jury to not take the testimony out of context. (Trial tr., Doc. #145, pp. 552-554, October 30, 2007). Failing to exclude or give a limiting instruction as to Petitioner's opinions as to legal conclusions regarding client and investor was prejudicial to Petitioner's defense, in and of itself. This prejudice was compounded by the district court's refusal to give the proper limiting instruction. The testimony was taken out or context by the jury. The jury was not told that Petitioner had testified in a civil case involving totally different issues.

CONCLUSION

By reason of the these errors, none of which the Opposition adequately addresses, further review should be accorded to Mr. Lay.

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Supreme Court, U.S.
MOTION FILED
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No. 10-695

In The

Supreme Court of the United States

MARK D. LAY,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

Petition For A Writ Of Certiorari To The United States Court of Appeals For The Sixth Circuit

BRIEF *AMICUS CURIAE* OF DR. BARRON H. HARVEY, DEAN OF THE HOWARD UNIVERSITY SCHOOL OF BUSINESS AND CHARLES R. ZAPPALA, ESQ.

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No. 10-695

IN THE SUPREME COURT OF THE UNITED STATES

MARK D. LAY,
PETITIONER,

V.

UNITED STATES OF AMERICA,
RESPONDENT.

MOTION OF DR. BARRON H. HARVEY, DEAN OF THE HOWARD UNIVERSITY SCHOOL OF BUSINESS AND CHARLES R. ZAPPALLA, ESQ. FOR LEAVE TO FILE BRIEF AMICUS CURIAE

Dr. Barron H. Harvey, Dean of the Howard University School of Business and Charles R. Zappalla, Esq., respectfully request leave to file their brief amicus curiae in this action. The brief was tendered on January 28, 2011, but has not been filed. It was believed that the brief was due on January 28, 2011, the date of the filing of opposition by the United States. It has now been clarified that the

amicus brief was due when the original Petition for Certiorari was filed. It is respectfully requested that the amicus brief tendered on January 28, 2011 be filed.

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served via US. Postal Service upon opposing counsel, on February 15, 2011.

The Honorable Neal Kumar Katyal, Acting Solicitor General
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TABLE OF CONTENTS

TABLE OF CONTENTS i

TABLE OF AUTHORITIES ii

STATEMENT OF INTEREST OF AMICUS 1

ARGUMENT 5

CONCLUSION 16

TABLE OF AUTHORITIES

Cases

Cleveland v. United States,
531 U.S. 12 (2000) 7

McNally v. United States,
483 U.S. 350, 356 (1987) 11

Neder v. United States,
527 U.S. 1, 25, 119 S. Ct. 1827,
144 L. Ed. 2d 35 (1999) 9, 10

Pereira v. United States,
346 U.S. 1, 98 L. Ed. 435, 74 S. Ct. 358 (1954) 7

Rewis v. United States,
401 U.S. 808, 812 (1971 13-14

Skilling v. United States,
561 U.S. _____ (2010), 130 S. ct. 2896
2010 U.S. LEXIS 5259
(June 24, 2010) 11, 12, 13, 14, 15

United States v. Bloom,
149 F. 3d 649, 655 (7th Cir. 1988) 13

United States v. Cohen,
518 F.2d 727, 737 (2 Cir) 7

United States v. Daniel,
329, F.3d 480, 487 (6th Cir. 2003) 10

United States v. Grossman,
843 F. 2d 78 (2d Cir. 1988) 7

United States v. Lane,
474 U.S. 438, 451 (1986) 6

United States v. Males,
459 F. 3d 154 (2d Cir. 2006) 8

United States v. Marando,
504 F.2d 126(2d Cir. 1974) 6

United States v. Maze,
414 U.S. 395 (1974) 7

United States v. Panarella,
227 F.3d 678, 692 (3rd Cir. 2002) 13

United States v. Pimental,
236 F. Supp. 2d 99 (D.C. Mass 2002) 11

United States v. Prince,
214 F. 3d 740, 748 (6th Cir. 2000) 5

United States v. Turner,
465 F.3d 667, 680 (6th Cir. 2006) 9

Statutes

18 U.S.C. §1341 . . . . . 3, 5, 6, 7, 9, 11, 14

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STATEMENT OF INTEREST OF AMICUS [1]

Dr. Barron H. Harvey is the Dean and Frank Ross/KPMG Endowed Professor in accounting at the Howard University School of Business. Dr. Harvey is a lifelong friend of Mr. Lay and a native of

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[1]In accordance with the provisions of Supreme Court Rule 37.6, it is hereby disclosed that counsel for Petitioner provided input to this brief of *amicus curiae* and also made a monetary contribution to the cost of printing. Other than counsel for Petitioner,no person other than the *amicus curiae* or their counsel contributed to preparation or submission of the brief. Pursuant to Rule 37.2(a), counsel of record for both parties received timely notice of amici's intent to file this brief. Letters from the parties consenting to the filing of this brief are on file with the Court.

Aliquippa, Pennsylvania. Dr. Harvey was a character witness at Mr. Lay's trial.

Under the distinguished leadership of Dr. Harvey, the Howard University School of Business has made strides in its ongoing quest to maintain excellence in its academic programs. The School's Undergraduate Program is ranked among the Top 75 US programs in Business Week's 2008 "Best Undergraduate B-Schools". It was among the top 20 schools in the Mid-Atlantic Region of the United States, 1 of 4 in the Washington DC Metro-Area and the only Historically Black University to be included in the ranking.

In the September 2007 *Wall Street Journal/Harris Interactive Survey* of corporate recruiters on business schools, the School's MBA program maintained its ranking as one of the top three national institutions for hiring minority graduates. Additionally, the 2007 Princeton Review, again ranked the MBA Program among the top business schools in the nation, *#1 ranking for the Greatest Opportunity for Minority Students and #5 ranking for Most Competitive Students*. The School is also ranked as one of the top 70 undergraduate business programs in the nation by *Businessweek* magazine.

In addition to the prestigious position as Dean of the School of Business, Dr. Harvey is a tenured member of the faculty and has served as a full professor in the Department of Accounting for over 18 years. In fall 2007, Dr. Harvey became the first endowed professor in the School of Business when he was named Frank Ross/KPMG Endowed Professor in Accounting. He has twice been named "Educator of the Year" by the National Association of Black Accountants Inc. (NABA).

By reason of his lifelong association with and his particular concern for fair treatment of African American professionals in the financial services sector, Dr. Harvey desires to bring to the attention of the Court the unprecedented and highly questionable nature of the theory underlying Mr. Lay's prosecution including the unjustified reliance on trade confirmation slips as the basis for prosecution under 18 U.S.C. §1341.

Charles R. Zappala is an investor/ businessman who has founded, acquired, developed and exited companies and projects ranging from plastics manufacturing to financial services. He was one of the founding principals of Russell, Rea, Zappala & Gomulka Holdings, Inc. ("RRZ&G"), the Pittsburgh-based investment

banking holding company. To date, the enterprise value of projects and companies developed and sold exceeds $500 million.

He is currently a Shareholder and a Director of several privately-held Companies, including CLT Efficient Technologies Group, an energy efficiency company; and OnQ Technologies, Inc., a residential structured wiring company.

He has served on various charitable boards, including Pittsburgh Youth Symphony, Pittsburgh City Theater, NCCJ and NEED. Mr. Zappala is a magna cum laude graduate of the University of Notre Dame with a Bachelor of Arts in Government, and an L.L.B. from Georgetown University Law Center.

Mr. Zappala is personally familiar with Petitioner and his work in the financial services industry.

ARGUMENT

As was point ed out in the dissent in the appellate court opinion in this action, in order to sustain a mail fraud conviction against Mr. Lay, the government was required to show proof of interstate mailing "in furtherance of the [alleged] scheme to defraud[.]" United States v. Prince, 214 F. 3d 740, 748 (6th Cir. 2000); see also, 18 U.S.C. §1341 (a mailing must be "for the purpose of executing such scheme or artifice" to defraud).

Here the charged mailings are "trade confirmation slips." The government did not contend and the evidence did not show that the slips themselves contained any misrepresentations or that they played any role whatever in parting the Ohio Bureau of Workers Compensation (OBWC) from its money. Instead, the slips simply confirmed trades that Mr. Lay made on the open market.

The dissent correctly points out that the governments' explanation of this point is amorphous at best. Post-fraud mailings, such as trade confirmations, can further a scheme if designed to lull the victims into a false sense of security, postpone their ultimate complaint to the authorities, and therefore make the apprehension

of the defendants less likely than if no mailings had taken place. United States v. Lane, 474 U.S. 438, 451 (1986). Here, there was no proof to support such a theory. In Mr. Lay's case, all of the trades were done correctly, which the government did not contest. The government alleged that the trade confirmations were used in a scheme to over leverage the Active Duration Hedge Fund (ADF). The evidence at trial however did not show how any of the trades accomplished over leveraging. The fact is many trades reduced leverage, and many trades were profitable. The government never distinguished this fact. The evidence did not address individual trades or the dates of the trades. Without showing the daily position of the fund and any losses generated by the trades, the confirmation slips in and of themselves did not advance the government's case.

The trade confirmation statements did not contain false information. In cases where mailing trade confirmation statements constituted a violation of 18 U.S.C. §1341, the statements were transmitted for the purposes of executing the artifice of scheme. See, United States v. Marando, 504 F.2d 126(2d Cir. 1974) where trade confirmation slips were mailed and determined to be an integral

part of a scheme to obtain property; also see, United States v. Grossman, 843 F. 2d 78 (2d Cir. 1988) where it was determined that:

> The mailings of the confirmation slips did further the purpose of executing the scheme. The confirmation slips (1) notified the relatives that the purchase or sale actually had been completed; (2) provided an on-going tally of purchases, allowing the relatives to cover each other's positions; (3) concealed the fraud by maintaining an appearance of normality, see, United States v. Cohen, 518 F.2d 727, 737 (2 Cir), cert denied, 423 U.S. 926, 46 L. Ed. 2d 252 (1975): and (4) allowed the relatives to demonstrate ownership after the recapitalization announcement. Pereira v. United States, 346 U.S. 1, 98 L. Ed. 435, 74 S. Ct. 358 (1954). [**27].

To establish a violation of the mail fraud statute, "the mailing must be for the purposes of executing the scheme." United States v. Maze, 414 U.S. 395 (1974). To state an offense under 18 U.S.C. §1341 this Court determined in Cleveland v. United States, 531 U.S. 12 (2000) that the evidence must

show that the defendant not only devised scheme or artifice, but also used that scheme or artifice to obtain money or property. See, United States v. Males, 459 F. 3d 154 (2d Cir. 2006) (Emphasis added). Here the evidence showed ADF received its first $100,000,000.00 before Mr. Lay ever executed a trade. There was no evidence that the mail was used to obtain money or property. There was no evidence that property or money was obtained through a scheme that involved the use of the mail. The trade confirmation slips here unlike those in Grossman or Mirando did not contain false information, did not document illegal insider trades, and were not transmitted to obtain money or property. The alleged nondisclosures and misrepresentations concerning leverage alleged by the government were not related to the mailing of confirmation slips. The trades reflected on the listed slips were lawful trades for a hedge fund. It does not matter that OBWC did not authorize them, the relevant private placement memorandum gave ADF's board sole discretion to deviate from the fund's leverage guideline, not OBWC. The trade confirmation statements report the purchases of securities on a certain date, from a certain broker, at a certain price. All of that

information was true, in every instance. On these facts a violation of 18 U.S.C. §1341 was not established.

Here OBWC invested funds in ADF on three discrete dates, August 20, 2003, May 21, 2004 and September 23, 2004. These are the only times OBWC "parted" with property.

> The mail fraud statute prohibits the use of the mails by any person "having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises..." 18 U.S.C. §1341. "Mail fraud consists of (1) a scheme or artifice to defraud; (2) use of mails in furtherance of the scheme; and (3) intent to deprive the victim of money or property." United States v. Turner, 465 F.3d 667, 680 (6th Cir. 2006). Materiality of falsehood is a requisite element of mail fraud. Neder v. United States, 527 U.S. 1, 25, 119 S. Ct. 1827, 144 L. Ed. 2d 35 (1999). The misrepresentation "must have the purpose of inducing [*7] the victim of fraud to part with the property or undertake some action that he would

> not otherwise do absent the misrepresentation or omission." United States v. Daniel, 329, F.3d 480, 487 (6th Cir. 2003). A misrepresentation "is material if it has a natural tendency to influence, or is capable of influencing, the decision of the decision-making body to which it was addressed." Neder, 527 U.S. at 16 (internal citation and quotation marks omitted).

McCauliff, supra.

There was no proof here that OBWC parted with property by reason of a material misrepresentation in a trade confirmation slip.

> The mail fraud statute "does not purport to reach all frauds, but only those limited instance in which the use of the mails is part of the execution of the fraud." Kann v. United States, 323 U.S. 88, 95, 89 L. Ed. 88, 65 S. Ct. 148 (1944). Accordingly, the government must show beyond a reasonable doubt that [defendant] caused the mailings listed in the indictment to be sent and th at the mailings were in furtherance of the fraud.

United States v. Pimental, 236 F. Supp. 2d 99 (D.C. Mass 2002).

Here there was no proof of any mailings in further of a scheme to exceed leverage or that the OBWC parted with money due to mailing trade confirmation slips.

On June 24, 2010, the United States Supreme Court in Skilling v. United States, 561 U.S. _____ (2010), 130 S. ct. 2896 2010 U.S. LEXIS 5259 (June 24, 2010) announced a seismic shift in mail fraud prosecutions. The appellate court totally ignored the Skilling opinion. The Skilling opinion highlights what the government's burden of proof is in a prosecution under 28 U.S.C. §1341for mail fraud. Skilling makes is clear that an essential element is a mail fraud prosecution is evidence of some form of gain or enrichment to the defendant. Skilling states:

> Enacted in 1872, the original mail-fraud provision, the predecessor of the modern-day mail and wire fraud laws, proscribed, without further elaboration, use of the mails to advance 'any scheme or artifice to defraud.' See, McNally v. United States, 483 U.S. 350, 356 (1987). In

> 1909, Congress amended the statute to prohibit, as it does today, 'any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises' §1341 (emphasis added); see id. at 357-358. Emphasizing Congress disjunctive phrasing the Courts of Appeals, one after the other, interpreted the term "scheme or artifice to defraud" to include deprivations not only of money or property but also of intangible rights.

Id. at *80-81 (emphasis added).

Skilling goes on to discuss the elements of an honest service fraud claim versus other frauds. In Skilling the Court pointed out the requirement for symmetry in a standard mail fraud case, that is the victim's loss of money or property supplied the defendant's gain with one the mirror image of the other. Id. at *82.

In this case it is undisputed that Mr. Lay did not realize any gain as a result of an alleged misuse of the mails. The OBWC's losses were due to unsuccessful attempts by Mr. Lay to recoup losses through increased use of leverage. In some instances gains resulted from the use of increased

leverage. In other instances losses occurred from its use. In no instance, however, did Mr. Lay realize any money or property from the use of allegedly excessive leverage.

Likewise, Mr. Lay has received no compensation from OBWC by reason of trading activity or volume. All of Mr. Lay's fees were paid by the ADF, not the OBWC. Mr. Lay received no compensation from OBWC for ADF trades. The absence of any gain of any nature by the Defendant is also fatal to a mail fraud prosecution. Skilling emphasizes this point.

The use of the excessive leverage was not a scheme to defraud. It was an investment strategy that failed. The purpose and intent of the strategy was not of a nature that could support a mail fraud prosecution. See, Skilling, (citing United States v. Bloom, 149 F. 3d 649, 655 (7th Cir. 1988) and United States v. Panarella, 227 F.3d 678, 692 (3rd Cir. 2002) (requires that a defendant act in pursuit of private gain)).

Skilling determined that a 28 U.S.C. §1346 prosecution requires as "offense conduct" evidence of either bribery or kickbacks and that the "ambit of criminal statutes should be resolved in favor of lenity." Id. at 100 (quoting Rewis v.

United States, 401 U.S. 808, 812 (1971)). The "offense conduct" in Mr. Lay's case which was a 28 U.S.C. §1341 prosecution according to Skilling, must include an element of gain at the expense of a victim, here OBWC.

In this case the gain element is totally lacking. The District Court stated in of Mr. Lay's sentencing memorandum:

> Looking back in hindsight, as the Court can do, it seems obvious that he should have stopped following the investment strategy he had in place. But at the time, no one had ever seen an instance in which rising bond process would not lead to a devaluation of existing bonds. But that is precisely what happened in this time frame. It was the first time in economic history of the United States that that occurred, and his strategy failed and because of the leverage, failed dramatically.
>
> ***
>
> It seems apparent that the defendant had not lost any monies for any clients in the management of the MDL investments until the defendant began excessive over-leveraging with

> the ADF. It appears from his past experiences with Mellon Bank and PNC the it was not the first time defendant took great risks in the belief that he could recoup his losses. The Court notes that the defendant, born in 1963, actively pursued a good education and did not demonstrate criminal tendencies. The defendant has no criminal record. The defendant appears to have been a responsible father. It does not appear to the Court that the defendant was motivated to gain more income by his management of the ADF.

(Trial Court Doc. #181 p. 23) (emphasis added).

As the District Court indicated, there was no evidence whatsoever that the mails were used by Mr. Lay in any scheme to defraud another or to generate gain for Mr. Lay. Skilling makes it clear the absence of this element is fatal to a mail fraud prosecution. The mailing of trade confirmation slips by third parties that document specific transactions did not result in any gain or benefit to Mr. Lay.

It is respectfully requested that the Court consider this information when reviewing Mr. Lay's Petition.

CONCLUSION

The amicus curiae here respectfully request that the Court grant certiorari.

January 28, 2011.

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181

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№. 10-695

Supreme Court, U.S.
FILED
DEC 29 2010
OFFICE OF THE CLERK

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TABLE OF CONTENTS

TABLE OF AUTHORITIES iii

STATEMENT OF INTEREST OF AMICUS 1

ARGUMENT 7

A. Mr. Lay's Relationship To The State Of Ohio Bureau Of Workers Compensation 7

B. Hedge Funds Are For Sophisticated Investors 14

C. The MDL Fund Was Designed To Be A Real "Hedge" 14

D. A Simple Bet On Interest Rates 16

E. MDL One Of OBWC's Most Successful . . 17

F. Why Invest More Money? 18

G. Investment Advisor Or Not 19

H. Mail And Wire Fraud 20

CONCLUSION 21

APPENDIX

APX A. Memorandum of OBWC, Chief Investment Officer James Scott McLean . . . . . .

APX B. Investment Management Agreement between Ohio Bureau of Workers' Compensation and MDL Capital Management, Inc. . . . . .

APX C. Investment Management Agreement between MDL and ADF . . . . . .

APX D. Consent of Acting Solicitor General to filing *amicus* brief . . . . . .

TABLE OF AUTHORITIES

Cases

Goldstein v. SEC, 451 F. 3d 873
(D.C. Cir. 2006) 13, 21

Statutes and Constitutional Provisions

Investment Advisers Act of 1940,
15 U.S.C. §80b-6 . . . . . 6, 7

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STATEMENT OF INTEREST OF AMICUS[1]

The individuals who have joined in the filing of this amicus brief are investment, academic and business professionals who desire to bring to the Court's attention an unprecedented employment

[1]In accordance with the provisions of Supreme Court Rule 37.6, it is hereby disclosed that counsel for Petitioner provided input to this brief of *amicus curiae* and also made a monetary contribution to the cost of printing. Other than counsel for Petitioner,no person other than the *amicus curiae* or their counsel contributed to preparation or submission of the brief. Pursuant to Rule 37.2(a), counsel of record for both parties received timely notice of amici's intent to file this brief. Letters from the parties consenting to the filing of this brief are on file with the Court.

by the United States of federal criminal securities laws to reach conduct by an African American investment manager, that when engaged in by non African American investment advisers heretofore, was treated as purely tortious, if anything. The conviction of Petitioner, Mark Lay, implies that it is a criminal offense for an African American investment adviser to lose a large sum of money in the market, notwithstanding the absence of theft, embezzlement or any form whatsoever of personal gain.[2] Mr. Lay was prosecuted for his handling of an investment by the Ohio Bureau of Workers Compensation (OBWC), that it is questionable that Ohio officials were authorized to make. There is a widely held perception that Mr. Lay's prosecution was racially and politically motivated and that Mr. Lay has been made a scapegoat for the misdeeds of certain high level Ohio officials. Accordingly, we desire for the Court

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[2]It should be noted that Mr. Lay received fees for his activity as a hedge fund investment adviser, but these fees were paid by the fund, not the investors. There was no churning allegation against Mr. Lay. Fees paid to Long Fund Advisers greatly exceeded those paid by ADF.

to review Mr. Lay's conviction as a matter of racial justice and fairness.

Set forth below is an individual list of the signatories with a description of their credentials and relationships to Mr. Lay.

1. Eric Carmichael Eric Carmichael has been in the investment industry since 1985. During his career he has actively been involved in both the investment banking and institutional brokerage sectors of the industry. In 1990, he established the Columbus, Ohio office for a national minority-owned investment firm.

   He provided brokerage services to the OBWC since 1992. He met Mr. Lay during the early 2000's and built both a friendship and business relationship whereby Mr. Carmichael's firm provided brokerage to MDL Capital Management.

2. Gerry Sherwin graduated from Columbia College in 1955 with concentration in Humanities and Government (Political Science). He served in US Army for two years and is currently a Marketing and Communications Consultant. He was formerly Senior Partner in Charge of Professional Development for six years at Bozell Group, has forty-five years of experience in Communications and

Marketing, and has held senior positions with Grey Advertising, Block Drug Company, Lehn & Fink, Bozell, WINS Radio.

Mr. Sherwin has known Mark Lay since he entered Columbia in 1981 when he was President of the Columbia Men's Basketball team and Mr. Lay was an undergraduate, and Captain of the men's basketball team. They continued their friendship after Mr. Lay graduated and stayed in touch whenever Mr. Lay came back to New York on business and to visit old friends. Mark Lay is someone Mr. Sherwin feels he can truly rely on--considerate, intelligent, are words that describe him--a friend of the highest order.

3. Pascal M. Nardelli, Managing Member, Castlebrook Development Group, LLC, Principal

4. Tracy Foster is the owner of P & W Foreign Cars and South Hills Audi, both located in Pittsburgh, Pennsylvania. Ms. Foster also owns Woodson Motor Sports in Ft. Wayne, Indiana. Ms. Foster has been a business associate of Mr. Lay for nearly a decade.

5. Bruce Goode is an investment banker and owner of Goode Investments located in Cleveland, Ohio.

6. Leroy Thompson is President/Chief Manager, BDT Development & Management, LLC, a real estate development and construction management firm with offices located in Pittsburgh, Pennsylvania and Knoxville, Tennessee. Mr. Thompson has known Mr. Lay for several years both personally and professionally. In all of our interactions, I have found Mr. Lay to be of sound judgment and character with the highest regard to professionalism. It is impossible for me to believe that Mr. Lay could have knowingly committed the serious crimes that he was charged and ultimately convicted of in federal court.

7. The Harvest Institute is a non-profit, tax exempt research educational, policy and advocacy organization located in Washington, D.C. and founded in 1993. Its mission is to engage in activities that lead to a Black America that is self-sufficient and competitive as a group within the next decade. Its founder is Dr. Claud Anderson, author of *Black Labor, White Wealth: A Search for Power and Economic Justice and PowerNomics: The National Plan to Empower Black America.*

The signatories to this brief have longstanding personal relationships with Mr. Lay.

It has been established unequivocally that Mr. Lay did not realize personal gain from the conduct which resulted in his conviction. However, critical exculpatory information probative of the political dimension to Mr. Lay's prosecution was excluded from evidence, namely a memorandum from the Ohio Bureau of Worker's Compensation Chief Investment Officer indicating that a high level cover-up of losses from OBWC investments took place. See, Appendix A. Also, included in this brief at Appendix B is the investment guideline applicable to OBWC investment advisors, which establishes tha the conduct for which Mr. Lay was prosecuted was not cognizable under the antifraud provisions of the Investment Advisers Act of 1940, 15 U.S.C. §80b-6, for the reason Mr. Lay was not an investment adviser to OBWC in relation to ADF and that Mr. Lay did not use the mails or wires in a scheme to defraud OBWC of money or property.

The signatories primary interest in this appeal is fairness. Losses in the marketplace, without more, historically have not resulted in criminal prosecutions and convictions in the financial industry. The Court should review Mr. Lay's case for the reason it stands out as an exception to the

treatment ordinarily accorded to investment advisers.

Lastly, the signatories urge review by the United States Supreme Court for the reason Mr. Lay's conviction represents an unprecedented extension of the Investment Adviser's Fraud statute, 15 U.S.C. §80b-6, to include claims by hedge fund investors against hedge fund advisers, and has created a conflict among the circuit courts of appeal.

ARGUMENT

A. Mr. Lay's Relationship To The State Of Ohio Bureau Of Workers Compensation

MDL Capital Management, Inc. (hereinafter "MDL") became an investment adviser to the Ohio Bureau of Workers Compensation ("OBWC") on May 14, 1998. See, Appendix B. Petitioner Mark D. Lay, was the Chairman and Chief Executive Officer of MDL. The agreement at Appendix B is the only investment adviser agreement between "OBWC" and "MDL".

In 2002 Petitioner formed the MDL Active Duration Fund ("ADF"). A separate investment adviser agreement was entered into between MDL

and ADF. See, Appendix C. Although OBWC invested in ADF, there was no investment advisers agreement between MDL and OBWC as it related to ADF for the reason it was known to both OBWC and MDL, that MDL would be ADF's investment advisor and that OBWC would merely be an investor in ADF. The investment advisers agreement between MDL and OBWC, Appendix B, specifically prohibited MDL, in its capacity as an investment adviser for OBWC, from investing OBWC funds in private placement securities such as ADF. In point of fact, the MDL-OBWC investment advisers agreement states, in pertinent part:

SCHEDULE A TO
INVESTMENT MANAGEMENT AGREEMENT

Client: State of Ohio, Bureau of Workers' Compensation Investment Manager: MDL Capital Management

INVESTMENT GUIDELINES
Active Duration Fixed Income Management

Statement of Purpose

The purpose of these guidelines is to:

establish the investment objective and performance standards of the Investment Account,

ensure that Investment Manager has the capability to evaluate the risk of all financial instruments in which the Investment Account is invested, and prevent Investment Manager from exposing the Investment Account to excessive overall levels of risk, exposure to inappropriate risk sources, or disproportionate exposure to any one risk source.

Investment Objective

The basic objective is to attain the highest total return consistent with a reasonable degree of risk by investing in fixed income securities. Success in achieving that objective will be measured by comparing the risk adjusted return and the after-fee return of the Investment Account to the Lehman Brothers Aggregate Bond Index...

Prohibited Securities

Dollar denominated foreign debt securities such as Yankees and Brady Bonds are prohibited

Securities denominated in currencies other than the U.S. dollar (non-dollar bonds) are prohibited

Private placements are prohibited except for 144A securities with registration

High yield securities are prohibited

> Use of inverse floaters, other exotic derivatives and reverse repurchase agreements is prohibited
> 144A securities without registration rights are prohibited
> Use of Eurodollar futures and options is prohibited
> Use of listed U.S. fixed income futures and options contracts is prohibited.

See, Schedule A, to Appendix B. (Emphasis added.)

Under the above guidelines Petitioner was not, in his capacity as an investment advisor for OBWC, permitted to invest OBWC funds into a private placement such as ADF. Accordingly, OBWC, a sophisticated investor, invested directly into ADF, in a series of separate and distinct investments that were not governed by Appendix B, but instead by the terms of a private placement memorandum ("PPM") and subscription agreement. It is clear from these documents, that MDL was not OBWC's investment advisor as it related to ADF and that OBWC knew it. OBWC, a sophisticated investor, had no investment advisor as it related to ADF, but wanted to take the risk of a hedge fund investment, on its own, as an overlay strategy.

The PPM that governed OBVC's investment into ADF made clear that MDL was not its investment adviser in relation to ADF. The PPM states:

> The Fund's investment adviser is MDL Capital Management, Inc. a Pennsylvania corporation ("MDL") or the "Investment Adviser"). The Investment Adviser will provide investment advisory services to the Fund and will be responsible for the overall management of the Fund's portfolio. The Investment Adviser is registered as an investment adviser with the U.S. Securities and Exchange Commission (the "SEC") under the Investment Advisors Act of 1940 (the "Advisers Act)|")...
>
> **DESCRIPTION OF THE ADVISORY AGREEMENT**
>
> The Fund has entered into an Advisory Agreement with the Investment Advisor. The Advisory Agreement provides that the Investment Advisor shall have broad discretion to direct and manage the Fund's investments. Subject to the approval of the Directors, the Investment Advisor may allocate all or a portion of the Fund's assets to the Master Fund, although it

is not required to do so. The compensation terms are set forth in "Charges to the Fund." The Investment Advisor may elect in its sole discretion, to defer payment of all or a portion of its Management Fee and Incentive Fees for a period of up to 10 years from the date payment is due. The Advisory Agreement also provides that the Fund will indemnify the Investment Adviser and its officers, employees and controlling persons from any liabilities, damages costs or expenses relating to the business or activities undertaken on behalf of the Fund, provided that such conduct does not constitute fraud, gross negligence, bad faith, willful misconduct, a willful material breach of the Advisory Agreement or will full violation of any material law, and provided that such indemnification obligation shall not apply to any liabilities, costs or expenses imposed on the Investment Advisor or its affiliates under the Securities Act (to the extent such indemnification would be contrary to public policy) or under ERISA. The Advisory Agreement further provides that the indemnified parties shall not be liable to the Fund in connection with its services in the absence of

> fraud, willful default, bad faith, gross negligence or reckless disregard of its obligations or duties under the agreement.
>
> In the Advisory Agreement, the Investment Advisor represents and acknowledges, among other things that (a) the Investment Advisor is a registered investment advisor, (b) that it is a fiduciary under ERISA with respect to ERISA plans investing in the Fund, (c) that it is a "Qualified Professional Asset Manager," (d) that it has complied and will continue to comply with applicable governmental regulations and (e) that it will not cause the Company to enter into any "prohibited transaction" under ERISA. Either party may terminate the Advisory Agreement on 90 days prior written notice to the other party.

Notwithstanding all of the above the Sixth Circuit, in conflict with every other court that has addressed this issue, most notably the District of Columbia Court of Appeals in Goldstein v. SEC, 451 F. 3d 873 (D.C. Cir. 2006) determined that Mr. Lay was the investment adviser to both ADF, a hedge fund, and OBWC, an investor in ADF. This finding is

unprecedented and threatens to cause chaos and uncertainty in financial markets.

B. **Hedge Funds Are For Sophisticated Investors**

Hedge funds by design and nature are for sophisticated investors. Because they are unregulated and have limited investors they require investors to meet (and sign off on minimum) standards or criteria. See, Subscription Agreement. For example, they require investors to be institutions, meet certain minimum net worth requirements (usually $1 to 2.0 million) or annual income of $200,000.00 or more. Id.

By mandating that these investors in hedge funds are indeed sophisticated, the hedge fund cuts down on the questions, concerns or servicing that a publicly traded fund might require. Further, they invite less scrutiny from any regulators or overseers as everyone is assumed to be "a big boy" and can take care of themselves and their interests.

C. **The MDL Fund Was Designed To Be A Real "Hedge"**

In addition to MDL, the Ohio Bureau of Worker's Compensation (OBWC) had dozens of investment managers who managed fixed income (bond) portfolios. These managers could invest in

bonds by buying them, collecting the interest payments, holding them to maturity or perhaps selling the bonds if they increased in value. These managers are referred to as "long only" managers.

ADF was designed to actually protect the OBWC bond portfolios as a hedge against falling bond prices which would therefore cause the bonds to lose principal value. It was a step OBWC took as a sophisticated investor however, not upon the advise of Mr. Lay.

Typically, when interest rates rise, the principal value (underlying value) of a bond would go down. Where a bond's interest rate is fixed (set) as other bonds yield more, they are worth more in the market.

ADF was by design allowed to use leverage (borrow money or securities) and allowed to go short (sell bonds which it did not own). With a short position, the investor is selling a security which he doesn't currently own; with the expectation that they will be able to buy the security back later at a lower price. As most people know, one of the best ways to make money as an investor is to "buy low and sell high." With a shorting strategy it is exactly the same except that the investor reverses the

traditional order and "sells high" first, then seeks to "buy low."

As shorting and leverage was not allowed for the other fixed income managers, they were expected to have a tough time in the market; if interest rates were to rise their portfolios were expected to lose money (principal). The original design of ADF was that it would make money to balance or hedge losses in the other fixed income portfolios managed by the other firms.

D. A Simple Bet On Interest Rates

During the time of the establishment of ADF, the Federal Reserve (at the time, headed by Mr. Alan Greenspan) was expected to raise short term interest rates.

In a typical yield curve environment, the longer money is invested, the more interest an investor would demand. So a six month investment would be a much lower yielding instrument than a two year investment and they would both be significantly lower yielding than say, a ten year investment.

Given these mechanics, when the Federal Reserve raised short term rates, then the natural assumption would be that longer term rates would also rise in some proportion to these shorter term

rates. Some market watchers would say they rose in sympathy to shorter rates.

Likely 90 to 95 percent of the time, this would make sense. As such, most investment firms and money managers made the same assessments and "bets" on the future directions of long term rates that Mr. Lay and ADF. Much like Mr. Lay and ADF, most of these firms on "The Street" lost money on the same trade, or with the same strategy.

Instead of rising significantly, or proportionally, the yield curve essentially "flattened" out, meaning that graphically, the spread or differences between short term and long term rates were smaller and the gap narrowed.

Even Alan Greenspan when asked by congressional questioners about this unusual interest rate movement lamented that he was as surprised and perplexed as every other market watcher was at the results.

E. MDL One Of OBWC's Most Successful

MDL had been one of OBWC's most successful fixed income advisers. MDL consistently out performed competitors in their asset class and out paced their assigned bench marks or comparable indices. The firm outperformed both

larger and smaller investment managers and institutions from around the country.

To a large degree, MDL was known to have a good understanding of the fixed income markets and known to make more significant "bets" in interest rates and the fluctuating prices of bonds. Fortunately for the OBWC these bets usually paid off handsomely.

F. Why Invest More Money?

Initially, OBWC invested $100 million in ADF. Given market conditions and the leverage used, this initial investment was lost in the market quickly.

After losing the first $100 million then additional allocations were made of another $100 million and $25 million more. History has shown that the vast majority of these funds were lost as well with OBWC retaining only about $9 million of the total money invested in ADF.

Most intelligent/logical people would agree that one would not make the second and third investments, if they felt that they were wronged. This would be especially true for seasoned investment professionals.

G. Investment Advisor Or Not

The prosecution of Mr. Lay under the antifraud provisions of the Investment Advisors Act, required Mr. Lay to be the investment adviser for OBWC in relation to ADF. OBWC was merely an investor into ADF. The failure of the Sixth Circuit to acknowledge and enforce this critical distinction portends chaos for financial markets. The Sixth Circuit has basically determined that notwithstanding clear language in a PPM and subscription agreement and the lack of an investment advisors agreement, if there is any history of an investment advisor relationship between a hedge fund investment adviser and an investor into this hedge fund, a jury or court may find that the investor is entitled to treatment as a client with all of the protections and restrictions applicable under federal securities laws to nonexempt investments. This conclusion totally undermines the rationale for Congressional recognition of the class of exempt investments known as hedge funds. The Sixth Circuit has ruled that hedge fund investors may have their cake and eat it too. That is, seek high rewards from a risky exempt investment, but then fall back on nonexempt regulatory protection if the investment

fails. The opinion of the Sixth Circuit in this connection is totally illogical. The Sixth Circuit opinion will create chaos in financial markets. It will cause investment advisors to be subjected to criminal liability for conduct in connection with exempt investment vehicles, specifically authorized by Congress to be formed for use by sophisticated investors capable of looking out for themselves. The Sixth Circuit opinion creates heretofore unknown criminal liability.

H. Mail And Wire Fraud

Petitioner's conviction should also be reversed for the simple reason OBWC did not part with money or property as a result of a use of the mail or wires in a scheme to defraud. OBWC parted with $225 Million dollars when it made three separate and distinct investments into ADF. Not when Mr. Lay conducted trades.

The prosecution of Mark Lay was nothing more than a means to make someone pay for the unfortunate losses that resulted from a failed investment strategy as far as ADF was concerned. OBWC's Long Fund continued to prosper and Mr. Lay continued as a Long Fund manager even after ADF was closed.

Given the allegations in the McLean memo at Appendix A and the Goldstein opinion, it is critical for the Court to accord further review to this case. It is unseemly for the securities law to be extended in the manner done here, where the defendant is a bright young African American, but the conduct that he is accused of engaging in never before resulted in prosecution.

CONCLUSION

The amicus curiae here respectfully request that the Court grant certiorari.

December 28, 2010.

s/Leo P. Ross, Esq.
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614-316-9144
Counsel for Amicus Curiae

APPENDIX

OTHER:

Memorandum of OBWC,
Chief Investment Officer
James Scott McLean . . . . . A1 - A38

Investment Management
Agreement between Ohio
Bureau of Workers' Compensation
and MDL Capital Management, Inc. . . . B1 - B30

Investment Management
Agreement between MDL and ADF . . . . C1 - C17

Consent of Acting Solicitor
General to filing *amicus* brief . . . . . D1 - D2

STATE OF OHIO
STATE PERSONNEL BOARD OF REVIEW

September 21, 2005

State Personnel Board of Review
65 East State Street, 12th Floor
Columbus, Ohio 43215-4213

Appellant:

James Scott McLean
7272 Black Abbey Court
Dublin, Ohio 43017
Home phone 614-760-0206
Cell phone 614-783-7200

versus

Appellee:

Ohio Bureau of Workers' Compensation
30 West Spring Street
Columbus, Ohio 43215-2256
1-800-644-6292

Notice of Appeal

Notice is hereby Given that Appellant appeals to the State Personnel Board of Review from the Order of Notice of Retaliatory Discipline - Whistleblowers;

which was received on September 7, 2005 and which was effective on September 7, 2005.

S/_____

Appeal to the State of Ohio - State Personnel Board of Review

Executive Summary

September 21, 2005

I was terminated as Chief Investment Officer at the Ohio Bureau of Workers' Compensation because of written reports and oral statements to disclose significant financial losses related to an external investment manager, MDL Capital.

Section 124.341 provides that a state employee who becomes aware in the course of his employment the misuse of public resources may file a written report identifying the misuse with his supervisor or appointing authority.

On June 1, 2005, I wrote a memo to the Administrator/CEO of the Ohio Bureau of Workers' Compensation, Mr. James Conrad, stating among other things that "It is important that the MDL Fund be reported accurately and the determination of the loss fully examined." This report was prepared based upon a request for "key projects" that needed to be addressed by the next

Administrator/CEO at the BWC. Mr. Conrad had announced his resignation and this was his last week as Administrator.

I was placed on Administrative Leave and then subsequently fired from my position at the Bureau of Workers' Compensation as Chief Investment Officer based upon my statements and written reports that identified my intent to disclose problems associated with investment in the MDL Active Duration Hedge Fund, problems that clearly related the misuse of public resources. Over the previous eight months (from approximately late September of 2004 to the date of my Administrative Leave (June 7, 2005), senior staff at the Bureau specifically directed the loss associated with this investment. My oral statements to these individuals and then written report to the Administrator/CEO that was shared with senior staff made it clear to these individuals that I was unwilling to cooperate any further in a deliberate "cover-up." These actions were crippling the ability of the Investment Department to function in a efficient manner and were themselves in misuse of public resources.

The reasons given in the termination letter that I received on September 7, 2005, from Tina Kielmeyer, the acting Administrator/CEO, citing a lack of effectiveness and poor decision making are false and not supported by the facts. When I asked for a single example of poor decision making, Administrator/CEO Kielmeyer cited my

allowing Investment Department staff to accept gifts of popcorn over the Christmas season. I told her that accepting popcorn was approved prior to its receipt by the Chief Legal Officer my direct supervisor and the Chief Ethics Officer at the Bureau. Ms. Kielmeyer then informed me that she had nothing further to discuss. My termination took less than ten minutes.

On April 17, 2005, I received an email from Administrator Conrad stating "I don't think I have told you recently, buy you are doing a great job under very difficult circumstances." "I really do appreciate your effort and rely on your knowledge." this was approximately 45 days before I was placed on Administrative Leave. It seems inappropriate and unjustified for a new acting Administrator/CEO to disparage my job performance and base her decision to terminate me after only two days when the previous Administrator/CEO never expressed a concern over my decision making or effectiveness.

I do not believe that it is a coincidence that I was placed on Administrative Leave the very same day that, after I was escorted from the building, the Bureau announced the problem with the MDL Active Duration Fund to the media.

I believe that I was placed on Administrative Leave because I made written and oral statements during the previous week that I intended to fully disclose

all problems associated with the MDL Active Duration Fund. I made it clear that I thought that the change in Administrator/CEO was an appropriate time to openly discuss the deliberate actions of senior staff at the Bureau of Workers' Compensation that prevented the disclosure of serious and potentially criminal activity that had taken place. I became a liability to the well orchestrated efforts by senior staff to shape their own version of the events that took place.

I was placed on Administrative Leave only two days after Ms. Kielmeyer had been appointed acting Administrator/CEO. I had no meetings or conversations with Ms. Kielmeyer prior to my being placed on Administrative leave and was given no reason for this action. I read in the newspaper that I had been placed on Administrative Leave to allow the Management Review Team "unfettered access" to the Investment Department records. The fact is that the Management Review Team, and the consultant employed by the Review Team, did not (based upon the conclusions and accusations that have been reported in the press) have access to the appropriate files and records that would have moved their investigation forward and have allowed for the truth to be uncovered about contested issues had I been allowed to continue to function in my capacity os Chief Investment Officer.

On the very same day that I was placed on Administrative Leave, June 7, 2005, and escorted out of the building, the Bureau announced to the press that it had a problem with the MDL Active Duration Fund. There is no doubt in my mind that the Bureau placed me on Administrative Leave to allow senior management to orchestrate the release of information to protect them from incrimination and to restrict my access to the information that would have demonstrated their involvement.

I have attached as Appendix I a memo that I provided to the Administrator James Conrad based on his request for the key issues that should be brought to the attention of a new Administrator. I made it clear to members of senior management both in this memo and in oral statements, including but not limited to Chief Legal Counsel and functionally my direct supervisor, John Annarino, that I would not let the Investment Department continue to suffer from the attempt to contain and cover-up the problems associated with the MDL Active Duration Fund.

The efforts to cover-up the problems with the MDL Active Duration fund were directly responsible for stalling the many needed changes that were necessary to increase the controls and reporting functions that needed to be put in place. Staff was continually to at bi-weekly staff meetings by Mr. Annarino that "no changes are going to be made"

and that "no one is going to lose their job or be laid-off" in an effort to keep any staff member from making statements to individuals outside the Department and in particular not to the press.

On at least two occasions, Mr. Annarino scheduled meetings with all of the individuals staff members that worked in the Investment Department to discuss his veto of potential changes. These individuals were upset that changes might impact their job responsibilities. Mr. Annarino met with me prior to these meetings to remind me that the Bureau did not want any possibility that a disgruntled worker might blow this whistle on the problems associated with the MDL Active Duration Fund. The two individuals that can attest to this are Kim Bamghn and Craig Philips, employees that met Mr. Annarino and myself and were told explicitly that no changes would be made to their job function without their consent. These individuals were assured that they would be given the opportunity to determine if they agreed or disagreed with any planned changes and have input into any changes. Staff was well aware that I had no authority to change their job functions or reprimand them for any perceived shortfalls or problems with their work product.

My attempts to reveal problems with the MDL Active Duration Hedge Fund date back to April 2005, when I schedule a meeting in my office with the CEO of MDL Capital, Mark Lay, I was

discouraged during a series of events that led to the continued deterioration in the investment in the MDL Fund from disclosing information beyond my direct superior/supervisor. I have included a description of events leading up to my being placed on Administrative Leave. I have also included copies of the few memos and emails that I have in my possession. I was never given access to my office, files or email once I was placed on Administrative Leave. My personal belongings were boxed up and placed on the loading dock the day I was terminated.

My goal is to be able to clear my name and reputation. My well publicized firing has significantly damaged my credibility and made it much more difficult for me to secure an appropriate job in my profession. The truth is that the State Insurance Fund and the ancillary investment accounts that I was responsible for were managed very effectively and profitably. I have been provided the resources that I need to dispute the allegations of the Management Review Team and their consultant.

While it may seem insignificant, I believe that there is an important clarification that should be noted in the termination letter that I received. Ms. Kielmeyer states that she encouraged me to "keep other investment options open." In fact, this is not what Ms. Kielmeyer told me. Ms. Kielmeyer told me that if the Management Review Team recommended

that the investment function be moved outside the Bureau, she was not certain that my job would be moved along with the transition of the investment accounts. Ms. Kielmeyer told me to keep all my options open, a much more general statement and one not focused on finding employment outside the Bureau.

The facts will reveal that I worked effectively, in cooperation with members of the Legal Department, Accounting Department, Internal Audit Department and Special Investigations and others, to identify and resolve the problems associated with the MDL Active Duration Fund. I advocated hiring a forensic account to follow the cash flows associated with the account. I was not included in the communication with the Ohio Attorney General, who I assumed was aggressively pursing all remedies to recover the funds lost in this investment scheme. I was told that the Attorney General was fully informed of the problem with the MDL Active Duration fund, but was excluded from any meetings or seeing any written communications.

I ask that the Ohio Personnel Board of Review find that the Ohio Bureau of Workers' Compensation acted contrary to the laws, policies and rules of the States of Ohio and take whatever steps it can to remedy the damages that has been done in James S. McLean.

Description of the Events and Issues Resulting in the Firing of James S. McLean, former Chief Investment Officer of the Ohio Bureau of Workers' Compensation.

Chapter One: Uncovering Problems with the MDL Active Duration Fund

On Friday, April 23rd, 2004, I met with Mark Lay, the CEO of the MDL Capital, in my office at the BWC in Columbus, Ohio, to discuss the management practices and investment strategy of the Active Duration Fund (Fund). I set up the meeting earlier the same week after reviewing the monthly performance reports for the MDL account for the month of March, which consisted of a fixed income component managed to an active duration mandate benchmarked to the Lehman Aggregated Fixed Income Index (probably the most common performance benchmark for fixed income in the institutional markets) and the Active Duration Fund (a hedge fund that is the focal point of the accusations of mismanagement and the cause of approximately $215 million in losses to the Bureau's State Insurance Fund). I arranged the meeting because the performance reports indicated that the Active Duration Fund had lost approximately $7 million in market value during the month of March (from approximately $102 million to $95 million). What was particularly unusual was not the magnitude of the loss but the fact that the Fund had lost value and not appreciated in value.

Mr. Gasper, my direct supervisor and Chief Financial Officer of the Bureau, had discussed the Fund with me prior to suffering a stroke that placed him on sick leave during this period. He explained that the investment in the Fund was intended to protect against losses in the core portfolio (the more stand "long only" fixed income assets managed by MDL) during periods of rising interest rates. In the March performance report that I reviewed, both the "long only" component of the assets managed by Mr. Lay and the Active Duration Hedge Fund had fallen in value during the month, a period in which interest rates had risen. Thus, it was the direction of the loss, and not the amount of the loss that triggered a red flag in my mind and led me to seek additional answers from Mr. Lay.

As I would discover only after my first several months of employment with the Bureau the investment in the Active Duration Hedge Fund was actually funded (the wire sent out to establish the account) during the first several weeks of my employment. Obviously the analysis and decision to make the investment in the Fund was made during the months prior to my arrival at the Bureau. While I was attending new employee orientation, investment staff was instructed to proceed with the funding. A wire was initiated by Mr. Gasper and signed off by senior investment department staff, Fred Zigler and Geoff Stafford, without my knowledge. I was not informed of the investment

at the time or for several months thereafter. In a very casual remark as I was walking by Geoff Stafford's cube one day, several months after I had been at the Bureau, Mr. Stafford mentioned to me that he thought the investment in the MDL Active Duration Fund was a bit unusual. I believe that he also went on to give me some of the history of the relationship between Mrk Lay, George Forbes and Mr. Forbes' daughter Mimi. I made a mental note of this, but didn't consider it particularly significant at the time given the difficult working relationship that Mr. Stafford had with the rest of the department staff, the problems that staff had expressed to me concerning Mr. Stafford and the impression that I had formed early on in my tenure with the Bureau that Mr. Stafford tended to create issues that had very little basis in fact. There was a long list of things in the Investment Department that Mr. Stafford had problems with, most of them with no basis. Several staff members had warned me that Mr. Stafford was making extremely derogatory comments about my leadership and decisions to other employees in the Bureau, employers outside the Investment Department that might not understand that this was just standard behavior for Mr. Stafford and the members of the Investment Department had basically learned to deal with.

Earlier in 2004 after I had been onboard with the Bureau for about six of seven months, I believe it was in February, Mr. Gasper suffered a stroke. Mr. Gasper was hospitalized for a short period of time

and was recovering at home during most of March and April to the best of my recollection. When Mr. Gasper suffered his stroke, it became incumbent upon me to dive into the files and get up to speed immediately on all the investments that I might not be fully familiar with after only my first six or seven months of employment (the Bureau had approximately 150 external investment managers/funds). One of the first files that I pulled was the MDL Capital file. I spent several hours reading the initial offering prospectus and other related documents that were in the file. Based upon that preliminary review, I believe that I had a good working knowledge of what I was dealing with. Based on this information, the overall portfolio (specifically a fairly conservative absolute rate of return strategy with a very conservative leverage ration of 150% or 0.5).

On either Thursday, April 22, 2004 or Friday morning April 23, I received phone call from Mr. Gasper. Mr. Gasper told me that he was aware that I was having a meeting with Mr. Lay and wanted to know why I was having Mr. Lay come over from Pittsburgh to discuss the Active Duration Fund. I explained to him that I had observed a drop in the value of the Fund from approximately $102 million to $95 million during the month of March which seemed inconsistent with the investment strategy as I understood it. Mr. Gasper told me that Mr. Lay was a "friend of the Bureau" and asked me if I knew that Mr. George Forbes (a member of the

Bureau's oversight commission) daughter "Mimi" worked for Mr. Lay. I explained to Mr. Gasper that the meeting was not intended to be confrontational, but that given his absence from the Bureau, I had stepped up my efforts to be able to answer any questions about all the components of the portfolio. I also explained that the monthly reports on the Active Duration Fund provided very little if any insight into how the account was being managed. In most case the monthly reports provided by outside investment managers offered "very detailed information on the specific holding - while the MDL Active Duration Fund was only reported as a single line item included in the report from MDL on the core portfolio position.

Mr. Lay and I met in my office on April 23rd. Mr. Lay explained to me that, based upon the recommendations of his professional staff, he had been convince to position the Active Duration Fund "long" during the month of March as opposed to being "short". He believed that despite his conviction that long-term interest rates would continue to rise, supported by the fact that the Federal Reserve Board of Governors had clearly signaled their intention to continue to raise short-term interest rates, he had been persuaded by his staff by a member of arguments and economic statistics to be "long." He stated that he had since reversed this position in the fund to be "short" and that the fund would continue to be short for the foreseeable future. He assures me that

he would consult with me if the position were to change for any reason. Again, it was my understanding that the primary, if not the exclusive reason for Mr. Lay being awarded the mandate for the Active Duration Fund, was to hedge his core position (his "long" core portfolio only and not the "long" fixed income of the Bureau) against rising interest rates. He admitted that he had been "whipsawed" during March (which means that he was on the wrong side of the market, changed sides, and then had that side of the market move against him). This was about the only explanation that seemed to me to make any sense prior to the meeting. His explanation was consistent with my suspicious about the account management.

At the meeting, I discussed the need to limit the volatility in the account, the importance of preservation of capital and need for much greater information flow about what was happening with the Active Duration Fund specifically. I told Mr. Lay that the single line item reporting that the Bureau was receiving was inadequate. He promised to send to the Bureau whatever detailed reports were necessary. He assured me that he never lost money for a client in his history as money manager and that the Bureau had been his first real breakthrough institutional account and was his most important client.

What I didn't know at the time was that Mr. Lay had to be aware of a continued loss in the fund

during the month of April which he did not disclose to me at the meeting on April 23. It wouldn't be until mid-to late-May, when I received the April performance reports from MDL that the Fund had suffered another loss during the month, a loss of approximately $35 million as I recall. When I reviewed the April report, I realized the Mr. Lay must have known about the loss at the April meeting and I felt that he had been dishonest with me by not disclosing the additional loss at that time. I called Mr. Gasper, who was still at home recovering from his stroke, and informed him of the loss and the lack of confidence I now had in Mr. Lay for being less than fully honest about the status of the account at the April meeting. Based on my lack of confidence in Mr. Lay and the importance for investment managers to completely honest in their relationships with the Bureau, I expressed my belief that the Bureau's continued investment in the MDL Active Duration Fund should be terminated at that time. Mr. Gasper informed me that he wanted to make some phone calls and think about the best way to deal with the situation.

Either later that same day or within a day or two of my conversation with Mr. Gasper, he called me back at the office and told me "here's what we're going to do," "We're going to give Mr. Lay an additional $100 million to manage in the Fund." Mr. Gasper told me that he trusted Mr. Lay and that Mr. Lay was, in his opinion, an experienced money manager that had the skills to successfully manage

this type of account. Mr. Gasper expressed his belief that long-term interest rates would almost certainly rise and that his was one of the few opportunities the Bureau had to mitigate the risks that rising interest rates posed to the "long" component that MDL managed. While I now suspect that the magnitude of the losses incurred during the month of April was tied to the over leveraging of the account, I was not receiving the additional reports that I had requested and the Mr. Lay had promised to provide. I went to Geoff Stafford following my phone call from Mr. Gasper and told him something such as: "you're not going to believe what we're going to do with the MDL Active Duration Fund." I told him that I had spoken with Mr. Gasper and that Mr. Gasper had directed be to transfer an additional $100 million from the core long component of the account to the Active Duration Fund. Mr. Stafford was aware of my discomfort in making the additional investment, and I believe that Mr. Stafford also had serious concerns with the management of the Fund. Mr. Stafford prepared the required paperwork, Fred Zigler signed the documents and copies were sent to Bank One (now J.P. Morgan/Chase and the Bureau's custodian bank) as well as to the Ohio Treasurer's Office informed them of the transfer.

At some point, I don't recall the exact date, Mr. Gasper and I had been discussing the increasing problems with the MDL Fund, I believe that it was in July or August of 2004. I had a one-on-one with the

Administrator (Mr. Conrad) later that afternoon and asked Mr. Gasper how to address the issue of the losses in the MDL Fund with Mr. Conrad. Mr. Gasper told me that the one-on-ones that I had with Mr. Conrad were not the appropriate forum to discuss the MDL losses. He told me that Mr. Conrad liked to focus on positive issues that he could put in the report to the Governor. Mr. Gasper assured me that he would address the issue with Mr. Conrad in a separate meeting. This was not the first time Mr. Gasper had "managed" the one-on-one process with Mr. Conrad. Prior to my first one-on-one (these took place about every two months or so) soon after being employed at the Bureau, Mr. Gasper had requested a meeting following the one-on-ones for my assessment of how the meeting went and what was discussed. There was no question that Mr. Gasper wanted to aware of all the issues that I discussed with Mr. Conrad and clearly instructed me on how he wanted to control the communication between myself and the Administrator.

It was common practice at the Bureau to never put anything sensitive or controversial in an email. Any and all sensitive issues were to be hand delivered to the appropriate individual or simply discussed and not committed to paper. The explanation on given was the email could become a public record and thus should be used for only the most bland ordinary correspondence. This was explained to me by Mr. Gasper and later

reinforced by John Annarino, the Chief Legal Officer and the Ethics Officer of the Bureau, when he became my direct report. In fact, Mr. Annarino would often chastise me for including his name on memo's that he thought discussed sensitive information and at one point instructed me how to "double-delete" emails from the computer system so they could not be retrieved later. This is somewhat tricky process that requires a series of steps and Mr. Annarino had the head of Special Investigations, Mr. Wersell, come down to my office on the 27th floor and show me the commands necessary to complete the process.

This is just an example of the environment in the Bureau that discouraged written reports on sensitive topics.

I was shown on e memo during my interrogation by the regulatory agencies I have met with where I sent a note to Mr. Gasper saying the approximate value of the MDL Fund was somewhere between $157 and $163 million, and he responded (somewhat sarcastically) that he liked the $163 number better. This memo, and I'm sure there is much more correspondence, illustrates that I was openly communicating with Mr. Gasper about the management of the Fund. This memo was probably dated during the summer of 2004 (June or July) based on the value of the Fund referred in the memo. As I recall, I had begun to get some scattered and sporadic reports on the MDL Active

Duration Fund, but not enough to be able to reveal what was really happening in the account. I believe that the July performance report showed another sharp decline in the value of the fund.

I discussed the continued deterioration of the Fund with Mr. Gasper and of course shared the monthly performance reports and any and all other correspondence that we had been received from MDL. Mr. Gasper told me that he would set up a meeting with MDL and that we would have Mr. Lay and all of the appropriate portfolio managers that had any responsibility for the accounts management come to Columbus for a meeting. As I recall this discussion took place in late July or early August and that we were forced to push the meeting back into September for some reason. I think the delay was an issue with MDL but I'm not sure.

I have a two page memo with a list of questions that I prepared prior to the meeting and shared with Mr. Gasper for his input and review before the meeting.

I need to go back at least a month here. I received a letter from Olympia Capital in Bermuda, the administrator for the Fund, asking me to sign an acknowledgment for certain "clarification" that were being made in the offering memorandum to the Fund. Once of these "clarifications" was to amend the limitation on the amount of leverage

used in the fund to exempt U.S. Treasury securities from the 150% leverage provision (U.S. Treasury securities were the only securities that the Fund was shorting in the account). In a phone conversation with Pricilia Brown, the Chief Legal Officer for Olympia Capital, I told her that I had no intention of signing the document because it was not a "clarification" but a material change in the investment strategy that I would never agree to. The letter dated August 2004, but I don't think I actually saw a copy of it until either late August or early September. At some point I was also provided with a redline copy of the changes to the offering prospectus. The way it was written and presented to me, it seemed pretty clear that they could not make the changes without my consent, which was never given, and they were clearly on notice that it would not be given.

Ms. Brown seem quite concerned that we would not sign it seems fairly obvious that she knew the account had suffered significant losses due to leverage that should not have been permitted by the administrator of the Fund.

Now back to the September meeting with MDL. Prior to the meeting with MDL, which began relatively late in the afternoon, Mr. Gasper came down to my office and told me that he had run into Mr. Conrad in the hallway on the 29th floor. According to Mr. Gasper, Mr. Conrad informed him that George Forbes, a member of the oversight

commission, had called him earlier that day, telling Mr. Conrad that he (Mr. Forbes) was aware that the Bureau was having a meeting with Mark Lay later that day and asking if we could possibly "do what you can to help Mark out" or "see if you can't give Mark a break, because I know he is having a tough time with the account." I'm not sure what the exact words were but it was something to this effect. This conversation, and actually all of the above conversations, is disputed by almost all of the participants. Did Mr. Conrad talk to Mr. Gasper and tell him about a phone call with Mr. Forbes? - I don't know. Mr. Conrad told me later (perhaps a week or two weeks later) that the conversation never took place.

What impact did Mr. Gasper's conversation with me have? I was relatively certain that prior to the conversation with Mr. Gasper, the ultimate outcome of the meeting with MDL would result in at least the termination of the Active Duration Fund if not the entire relationship with MDL Capital. Now, I was being told that the Administrator wanted us to "give Mark Lay a break." I was somewhat disappointed that Mr. Lay was going to get a break that I felt he didn't deserve, but at the same time I felt absolved of any responsibility for what might happen to the Fund going forward. The responsibility for the Fund would now be assumed by Mr. Conrad, Mr. Gasper and others. I also thought that my suspicious that perhaps Mr. Gasper was not keeping Mr. Conrad fully informed about

the problems with the active duration Fund were unfounded, and obviously Mr. Conrad had been in the loop and the assurance that I had received from Mr. Gasper that he would discuss it with Mr. Conrad "in the right forum and not in a one-on-one" had been followed up on.

In the meeting Mr. Lay asserted that "he thought we had signed" the "clarification" from Brown Capital. When informed that we had not signed the acknowledgment to allow for increased leverage, Mr. Lay said something to the effect of "-well then I guess I'm in a lot of trouble." Mr. Lay contended that interest rates would move up and the Fund would ultimately prove to be profitable. Nothing was really resolved in the meeting. I told Mr. Gasper that I didn't think Mr. Lay was being honest about not knowing that we had not agreed to the "clarification" in the leverage provision, and that what type of manager would commit hundreds of millions of dollars, actually almost $2 billion at that point to an investment strategy that he "thought" was approved!

Within a period of about two weeks (very approximate) I received a call telling me the Administrator wanted to see me in his office. Apparently, someone in the Bureau (an employee of Financial Reporting I have been told) informed Tina Kielmeyer, then the assistant administrator, of the losses being recognized in the MDL Fund. Apparently, this individual had been talking with

someone in the investment department, although Financial Reporting had ready access to the information themselves. The topic was not hidden from staff within the investment department. At the same time I was meeting with Administrator Conrad, three investment department staff were reporting "something strange going on with the MDL account" to internal investigations within the Bureau. The staff members told me this after their meeting. They told me that it was not their objective to get me in trouble, they wanted to get Geoff Stafford in trouble. In general, everyone in the department couldn't stand Mr. Stafford.

During my meeting with the Administrator, I told Mr. Conrad that I assumed he was aware of the problems with the MDL Fund through his conversations with Mr. Gasper. Mr. Conrad informed me that he never spoke with Mr. Gasper that afternoon in the hallway on the 29th floor and had never received a phone call fro Mr. Forbes concerning the MDL account. I was instructed not to talk to Mr. Gasper. I found out later that afternoon that Mr. Gasper had been placed on Administrative Leave and had left the building.

Either the next day or perhaps two days later, I was called back into Mr. Conrad's office and asked to think very carefully before I answered the next question. Was I sure that Mr. Gasper had told me the Mr. Conrad had received a call from George Forbes to go easy on Mark Lay? Did Mr. Gasper

perhaps tell me that he (Mr. Gasper) had received the call from George Forbes? I thought very carefully about my answer, but there was no doubt whatsoever in my mind what events had taken place. Mr. Gasper had told me that he and Mr. Conrad had discussed the MDL Active Duration Fund in the hallway on the 29th floor and Mr. Gasper told me the Mr. George Forbes had called Mr. Conrad to ask us to go easy on Mark Lay. Whether Mr. Gasper and Mr. Conrad really had this conversation I may never know. Mr. Conrad denies it. It is my understanding that Mr. Gasper denies it.

The next day or two, I found out while at a meeting in Zanesville on Bureau business from Mr. Conrad's assistant, Mr. Ben Taylor, the Mr. Gasper had resigned. All this took placed during my first year (or about 13 months) at the Bureau.

Chapter Two: Mr. Gasper Leaves the Bureau and the Cover-up of the MDL Mess Begins

With Mr. Gasper's departure, the line of reporting for me switched to Tracy Valentino, who was made acting Chief Financial Officer. This reporting structure only lasted for a few months, and functionally I started to have more frequent one-on-one's with the Administrator, Mr. Conrad, and did not have a great deal of interaction with Ms. Valentino. When Ms. Valentino was promoted to Chief Financial Officer from "acting" I was told that

I would report directly to Mr. Conrad, with John Annarino, the Chief Legal Officer, my direct supervisor for all administrative matters. Functionally, I began reporting to Mr. Annarino and not Mr. Conrad. Even Mr. Annarino was somewhat confused about the overall structure, he certainly considered me a direct report to himself and not Mr. Conrad. I did continue to have periodic one-on-one's with Mr. Conrad, but met with Mr. Annarino practically daily on a wide range of issues. Mr. Annarino began attending Investment Department staff meetings and met one-on-one with every member of the investment department staff.

Mr. Annarino also the Chief Ethics Officer for the BWC, coordinated what I can only refer to as the "cover-up" of the MDL losses. I assume that he was directed by the Administrator to keep a lid on the MDL problem, but I don't have any documentation Mr. Annarino was particularly concerned that someone in the investment department would contact the press or somehow provide documents or information on MDL to someone outside the Bureau. Mr. Annarino made frequent statements at every investment department staff meeting that "no one was going to lose their job or get laid off" and that "there were not going to be any changes in anyone's job that they didn't agree with." Mr. Annarino directed me to give annual performance reviews to staff that rated them as high as possible in every category. Several staff members were

disappointed the previous year that they had achieved only "satisfactory" ratings on their annual performance reviews. He also made frequent statements that the investment staff were "the finest in the industry" and the best performing department at the Bureau. Every time I tried to review operational processes or make any changes, staff always threw this back in my face, that they were "already the best they could be" and why should they put forth any extra effort to change anything. Mr. Annarino made it very clear to the staff that I did not have authority to discipline them in any way - and they took advantage of this. I wrote a reprimand for Fred Zigler after he refused to have anything to do with compiling and verifying performance reporting for the outside managers, even though this was one of the key responsibilities in his job description. Mr. Annarino refused to let me even finish the final draft of the reprimand.

Mr. Annarino instructed me to make sure the staff was kept content and happy so that they would not reveal any information on MDL. Keeping a lid on the MDL losses was not something that I simply assumed that Mr. Annarino wanted: it was a direct and straightforward mandate. The Bureau did not want any information on MDL to get out and I was to cooperate with the mandate.

The Bureau also deliberately misled the auditors, KPMG, so that the problems with MDL would not be

included in the then just finished audit of the 2004 fiscal year. The lead auditor on the BWC account called to inquire about the departure of Mr. Gasper and asked whether it was related to anything that his firm should be aware of. The Partner at KPMG was told "no" that Mr. Gasper had left for health related reasons only.

During the initial "pre-meeting" for the fiscal year 2005 audit (audit period June 04 - June 05) the heads of the departments that would work most closely with the audit team and key staff members in those departments met with and were introduced to the various auditors that would be working on the audit. As the meeting was wrapping up, I was concerned that the MDL issue had not been discussed. I wrote the letters "MDL" on the top of a legal pad and walked over to the Chief Financial Officer, Tracy Valentino, pointed to the letters and said ' don't you think it's important that we discuss this issue?" Ms. Valentino told me that she had already discussed the issue in her office with the partner in charge of the audit for KPMG and that it was "taken care of." The objective was to sufficiently bury the losses in the footnotes so that the issue would not appear as a significant issue. The message to me at the meeting was that MDL was not an issue to be discussed openly during the audit. This meeting took place (approximately) in May of 2005.

The "cover-up" of the MDL losses became increasingly frustrating because it was during this period that I was lobbying in the strongest possible manner for extensive changes within the investment department that would begin to guild an infrastructure adding technology, staff and due diligence procedure that would not allow this type of loss to go unnoticed going forward. This is well documented in the budget process that took place in the Spring of 2005.

Chapter Three: Overall Job Performance

The termination letter that I received from Administrator Kielmeyer stated that "your leadership of the investment department of the BWC does not meet my expectations." The facts will show that I only worked for Administrator Kielmeyer for two days before I was placed on Administrative Leave. It went on to say that "Your lack of effectiveness, and poor decision making has only led me to conclude that it is now time to move the investment operation at BWC in a new direction with new leadership." This was the first time I had been confronted with accusations of "lack of effectiveness" and "poor decision making."

Less than two months before I was placed on Administrative Leave, I received an email from then Administrator Conrad dated April 17, 2005 stating "I don't think I have told you recently, but

you are doing a great job under very difficult circumstances." "I really do appreciate your effort and rely on your knowledge." This is one of the few documents that I do have access to after being escorted from the building upon being placed on Administrative Leave.

I asked Administrator Kielmeyer in the very short meeting (probably less than ten minutes) that I had with her on September 7, 2005, to give me an example of a "poor decision" that I had made while Chief Investment Officer. Her first response was that I had allowed the investment department staff to accept "meat trays and wine" as gifts from investment manager and brokers doing business with the Bureau. I told her that the staff did not accept any " meat trays" or bottles of wine while I served as the Chief, and that she was referring to events that took place prior to my employment at the Bureau. I had heard stories of somewhat excessive Christmas gifts from brokers prior to my arrival at the Bureau and told her that in fact I had sent out a very stern letter several months prior to the Christmas season explaining to the brokers and investment managers the policies that we operated under at the BWC and not to send any gifts. She then told me that I had allowed staff to accept popcorn. When I explained to her that I had discussed the acceptance of these consumable gifts with Mr. Annarino, the Chief Legal Officer and Chief Ethics Officer of the Bureau, and he agreed that it was allowed under Bureau

policies to accept these types of gifts as long as they were shared with the rest of the staff and Bureau at large, which they were. She then responded that "that's the difference between you and me" because she did not think it was appropriate for the investment staff to accept popcorn from individual doing business with the Bureau. She then went on to bring up the MDL situation making a comment similar to "and the whole MDL mess." I replied that I had in fact worked to uncover the problems with the Active Duration Fund at a very early stage and had reported it to my superior. At that point she said she had nothing further to say and turned it over to Barb Young. Director of Human Resources.

Ms. Young told me that I would be getting my last paycheck on September 17, for time already worked, that today (September 7) was my last day and that I would get paid vacation and half of my accumulated sick leave. The whole meeting lasted about ten minutes or less. At that point, Tom Wersell, head of Special Investigations, opened the door and met me at the loading dock with my personal belonging that were in my office boxed up.

I would like to address the accusation of a "lack of effectiveness." During the approximate two years that I served as Chief Investment Officer at the Bureau, the State Insurance Fund exceeded its performance benchmark. During fiscal year 2005,

even after accounting for a least $200 million in losses due to the MDL Fund, the State Insurance Fund more than likely (I haven't seen the June 2005 performance numbers) exceed its performance benchmark for the fiscal year by significant margin, perhaps 50 basis points, one of the larger margins of out performance in Bureau history. While these figures are being disputed by the Management Review Team and their consultant, the real performance numbers will be revealed once a through and accurate assessmen of the State Insurance Fund's performance is conducted. The statement on performance that have been released to the press are simply wrong. The ancillary accounts, which I personally managed, and represented about $1.4 billion, exceeded the Lehman Aggregate Fixed Income Benchmark by almost 70 basis points over the past year, better than the majority of fixed income managers employed by the Bureau and most likely in the top 10 percentile of fixed income managers over the same period.

I put in place a program to have J.P. Morgan/Chase provide comprehensive performance reporting a significant deficiency that existed when I arrived at the BWC. The transition from the legacy Bank One system to the J.P. Morgan/Chase system was being implemented as quickly as possible. I had involved the Chief Financial Office, Tracy Valentino, who wen with me to the meeting at J.P. Morgan/Chase at their

Polaris offices to see a demonstration of the new system and she had approved funding it in the Bureau budget.

I submitted a budget that requested six additional professional staff be added to this investment department along with over $1 million in additional software to expand and enhance the ability of the department to conduct investment analysis and due diligence. When I arrived at the BWC, there was really no capacity to do appropriate analysis and the reporting system were focused on accounting functions and not investment analysis. The accounting system was not capable of accurately recording the investment transactions that were being conducted by some of the largest outside investment managers.

I significantly reduced the funds under management by underperforming managers, including National City and Fifth Third Bank, bringing the balances of these two managers down to approximately $50 million from balances that had been in excess of $200 million and $100 million respectively. The consultant brought in by the Management Review Team contemporaneously with my being placed on Administrative Leave (Ennis Knapp) claimed credit "firing" these same managers. The same credit was taken for two American Express funds that I had recently reduced by 50%. The consultant, Ennis Knapp, announced to the press that they

were firing these managers claiming the credit for uncovering problems with the manager. I had in fact "fired" a number of managers for various compliance or performance issues over the two year period that I was there.

These sharp and significant reductions in funds managed by some of our outside investment managers came during a period when I was under direct instructions from my supervisor, Mr. Annarino, to "make no changes." This direction was in place for the last nine months or so that I was the Chief Investment Officer. There were constant and multiple requests for the release of public information by the media concerning the Capital Coin funds that severely stretched the resources of the investment department beyond its ability to perform. In spite of an operating environment that did not have sufficient resources to excel, the monthly performance reports, the analysis of the RFP's that were issued, fixed income trading, and all the extensive duties and operations of managing am multi-billion portfolio continued without significant problems. Even with the directive to "make no changes" I continued to push for numerous improvements and innovations in the operations of the investment department.

There are subtle but important issue that I want to address that was included in my Termination Letter. Administrator Kielmeyer told me at a meeting that I requested while I was on Administrative Leave to

keep my options open not other employment options as highlighted in the letter. Administrator Kielmeyer indicated that if the decision of the Management Review Team was to move the investment operations outside of the Bureau, then my position might be at jeopardy. At no time during this meeting did she indicate any displeasure or problems with my past performance or decision making.

I have a copy of a memo that I sent to Administrator Conrad during his last week as Administrator based upon his request to compile a list of "key projects" underway in the investment department. In the memo I identify the ongoing investigation of MDL at the number one key project that was impacting the Investment Department. The memo was prepared to inform the next Administrator/CEO of the most immediate issues at the Bureau that should be addressed. I clearly stated that "It is important that the MDL Fund be reported accurately and the determination of the loss fully examined." The memo goes on to explain a number of projects that were underway all dealing with enhancements to controls and increasing the abilities and transparency of many of the issues that I seem to be accused of not addressing.

I believe that this memo alerted senior management to the fact that I was unwilling to continue to participate in any "cover-up" of the

MDL Active Duration Fund problem. I made it clear in my conversations with Mr. Annarino and others that once a new Administrator was hired, that it had to be made public. I don't believe that it is a coincidence that within hours of my being sent home on Administrative Leave that the Bureau announced to the press that there was a problem with the Pittsburgh based investment manager, MDL Capital.

Chapter Four: My Expectations from the State Personnel Board of Review

My goal is to be able to clear my reputation. I have been accused of being ineffective and making poor decisions. This is simply not true. I want to clear my name to be able to secure continued employment in relatively small community of individual investors. The decisions to invest in the Capital Coin funds and the MDL Active Duration Fund were made before I arrived at the Bureau. There was no complacency on my part to review, analyze and challenge to continued investments in these external investment managers. In the case of the Capital Coin fund, internal auditors at the Bureau had raised questions about the procedures and controls that were in place and were rebuffed by senior management. The Capital Coin funds underwent financial reviews by what was assumed to be an independent certified public accounting firm.

The Bureau has a Financial Reporting unit, Internal Audit and undergoes a full audit annually by KPMG. The separation of duties and responsibilities is a critical component to insure proper controls and oversight. There was no effort by the Investment Department to discourage a full and complete accounting of my investment, investment manager or broker/dealer.

I firmly believe that I was placed on Administrative Leave and subsequently terminated from my position at the Bureau based upon my statements and written report to bring the issues in the MDL Active Duration Fund to the attention of the next Administrator/CEO and to advocate for full disclosure.

The reasons given for my termination, a lack of effectiveness and poor decision making are not supported by the facts and are not true. Prior to my termination, I was never notified of any poor decisions that I had made or any lack of effectiveness. In fact, I have included an email from the former Administrator/CEO stating just the opposite.

I have cooperated with all of the various legal and regulatory agencies that are currently investigating these issues. I have answered every question honestly and have tried to provide as much information as I can to allow these agencies to identify and prosecute any wrongdoing. I estimate

that I've given about 35 hours of testimony to date, all with any legal representation. I've told the truth and I don't believe that I'm suspected of any wrongdoing and I shouldn't be!

The Bureau did not give me an opportunity to resign, thus I'm first person that has been "fired" from my involvement with the current scandals impacting the BWC. I believe that I was "fired" for threatening to bring the truth out in the open. I don't think this right.

The Bureau has allowed the Management Review Team and their consultant to make numerous defamatory statements to the press that have no basis in fact. They have mad statements to the next Chief Investment Officer needs to be "ethical and competent." These individuals have never met with me and do not know me.

I ask the State Personnel Board of Review to remedy this injustice. I just finished putting one daughter through college and have another daughter in her second year at Ohio University. I want to show them that people shouldn't be punished for doing the right thing.

INVESTMENT MANAGEMENT AGREEMENT
between
OHIO BUREAU OF WORKERS' COMPENSATION
and
MDL Capital Management, Inc.

This is an Agreement by and between MDL Capital Management, Inc. (hereinafter referred to as the "Investment Manager"), doing business at 225 Ross Street, Third Floor, Pittsburgh, Pennsylvania 15218, Bureau o Workers' Compensation (hereinafter referred to as the "Bureau"), having offices at 30 W. Spring Street, Columbus, Ohio 43215-2256, entered into the day, month and year set out below.

Whereas, the Bureau has issued as Request for Proposal (897007) for fixed income investment fund managers; and

Whereas, the Investment Manager has submitted one of the lowest responsive and responsible proposals to the Bureau's RFP and was chosen based upon investment performance standards established by the Bureau as well as organization strength, investment background and the ability to conform to the Bureau's Investment Policy and Guidelines; and

Whereas, the Bureau desires to enter into and Agreement with the Investment Manager to provide the needed services as set out in the RFP:

Now, therefore, the parties hereto mutually agree to the following provisions:

1. **Appointment as an Investment Manager**. The Bureau appoints and retains the Investment Manager as a discretionary investment manager to the Bureau on the terms and conditions set forth in this Agreement and the Schedules attached hereto for those assets that the Bureau assigns, which assets shall be referred to collectively as the "Investment Account". The Investment Account assets shall remain a part of and subject to the provisions governing the individual trust funds and at all times shall be held exclusively for the purposes for which the funds are collected. Subject to the investment objectives, policies, and restrictions set forth in this Agreement and the Schedules attached hereto, the Investment Manager shall have full discretionary authority to manage the Investment Account, including, when the Investment Manager deems appropriate and without prior consultation with the Bureau, the investment and reinvestment of assets in the Investment Account. The Bureau may make additions to and withdrawals from the Investment Account in such amounts as the Bureau shall deem appropriate, provided hat all withdrawals shall be made after giving the Investment Manager notice as set forth in Schedule A.

2. **Acceptance of Appointment; Standard of Performance**. The Investment Manager accepts its appointment as a discretionary investment manager and agrees to use it best professional judgment to manage and invest the Investment

Account in accordance with the provisions of this Agreement. The Investment Manager acknowledges that the Investment Account assets are those of the public trust fund governed by the provision of Chapter 4123, Ohio Revised Code, and governed by the Statement of Investment Policy and Guidelines. The Investment Manager acknowledges receipt of a copy of Ohio Revised Code Chapter 4123 and a copy of the Statement of Investment Policy and Guidelines and agrees to adhere to the standard of care and conduct required of a fiduciary under Chapter 4123 and any applicable federal and state law.

3. Investment Objectives, Policies, Modifications and Restrictions. The investment objectives, policies and restrictions of the Investment Account are set forth in Schedule A of this Agreement and may be modified by the Bureau with sixty (60) days prior written notice to the Investment Manager. The Investment Manager shall promptly advise the Bureau of its disagreement in writing with any modifications to Schedule A proposed by the Bureau. Any termination shall be in accordance with the provisions of Paragraph 17.

4. Transaction Procedures. All Investment Account transactions shall be consummated by payment or delivery to or by the custodian, currently the Treasurer of the State of Ohio ("Custodian"), through the Custodian's Agent ("Custodian's Agent") or such depositories or agents as may be

designated by the Custodian, of all cash and/or securities due to or from the Investment Account. Except as provided above, the Bureau shall be responsible for all custodial arrangements and the payment of all custodial charges and fees and the Bureau shall be responsible for giving proper instructions to the Custodian. The Investment Manager shall have no responsibility or liability with respect to custodial arrangements or the acts, omissions or the conduct of the Custodian except where (1) the Investment Manager participation in or undertakes to conceal an act or omission of the Custodian where such act or omission is a breach of Custodian's or Investment Manager's fiduciary responsibilities, (2) by failure to discharge its responsibilities under this Agreement, the Investment Manager has enabled the Custodian or Bureau to commit a breach of Custodian's or Bureau's fiduciary responsibilities, or (3) the Investment Manager has knowledge of a breach by the Custodian or Bureau and does not make reasonable efforts under the circumstances to remedy the breach of Custodian's or Bureau's fiduciary responsibilities and is under a duty to do so. With regard to the foregoing power and duties, the Bureau acknowledges that the Investment Manager shall have no responsibility for the failure by the Custodian to make timely settlement of transactions in securities that have been loaned from the Investment! Account by the Custodian pursuant to a securities lending program authorized by the Bureau. The Bureau further acknowledges

that the Investment Manager shall have no obligation or responsibility to vote proxies for securities loaned from the Account by the Custodian.

Notwithstanding the provisions of this paragraph, all transactions shall be carried out pursuant to Schedule C.

5. Procedures for Securities Transfer. Procedures for the transfer of securities and cash to and from the designated Investment Account under the terms of this Agreement shall be set forth in a directive letter from the Bureau prior to any transfer. The Investment Manager agrees to follow these procedures.

6. Allocation of Brokerage. The Investment Manager shall have the authority and discretion to select brokers and deals to execute Investment Account transactions initiated by Investment Manager, and for the selection of markets on or in which the transactions will be executed. The Investment Manager may allocate the execution of transactions to such brokers and dealers for execution on such markets, at such prices and at such commission rates as in the good faith judgment of the Investment Manager will be in the best interest of the Investment Account, taking into consideration in the selection of such brokers and dealers not only the available prices and rates of brokerage commissions, but also other relevant factors (such as, without limitation, execution

capabilities, research services provided by such brokers and dealers which are expected to enhance the Investment Account and overall management capabilities of the Investment Manager). The Investment Manager shall not execute Investment Account transactions through or with affiliates of the Investment Manager. The Bureau will provide the Investment Manager with a list of approved broker and dealers to be sent in letter form which will require acknowledgment of receipt. The use of Approved Brokers is required by the Bureau's Investment Policy which also mandates the amount of transactions to be done by minority and Ohio qualified brokers.

7. Proxies. The Investment Manager shall use its best good faith judgment to vote such proxies in a manner which best serves the general provisions of the Ohio Revised Code and the interest of the Bureau.

8. Reports. The Investment Manager shall provide to the Bureau monthly and quarterly reports concerning the status of the Investment Account and all other reports set forth in Schedule A and all reports as may be customary or reasonably requested by the Bureau.

9. Service to Other Clients. It is understood that the Investment Manager performs investment management services for various clients. Subject to the provisions of paragraph 2 hereof the Bureau

recognizes that the Investment Manger may give advice, exercise investment responsibility and take action with respect to any of its other clients which may differ from advice given or the timing or nature of action taken with respect to the Investment Account so long as the Investment Manager's policy to the extent practical, is to allocate investment opportunities to the Investment Account over a period of time on a fair and equitable basis relative to other clients.

It is understood that the Investment Manager shall not have any obligation to purchase for or sell for the Investment Account any security which the Investment Manager, its principals, affiliates, or employees may purchase or sell for its own or for their own accounts or for the account of any other client, if in the opinion of the Investment Manager such transaction or investment appears unsuitable or undesirable for the Investment Account.

No personnel of the Investment Manager, who exercises any functions or responsibilities in connection with the review or approval of the undertaking or carrying out of any work under this Agreement, shall prior to completion of said work, voluntarily acquire any personal interest, direct or indirect, which is incompatible, or in conflict with the discharge and fulfillment of such person's functions and responsibilities with respect to the work under this Agreement.

Any such person who acquires an incompatible or conflicting personal interest, prior to, on or after the effective date of this Agreement,

or who involuntarily acquires any such incompatible or conflicting personal interest, shall immediately disclose his or her interest to the Bureau in writing. Thereafter such person shall not participate in any action affecting the work under this Agreement, unless the Bureau shall determine that in the light of the personal interest disclosed, such person's participation in any such action would not be contrary to the public interest.

10. Assignment and Subcontracting. No "assignment" (as defined in the Investment Advisers Act of 1940) of this Agreement shall be made by the Investment Manger without the written consent of the Bureau. If the Investment Manager merges or consolidates or transfers substantially all of its assets to another entity, the resulting entity shall so notify the Bureau and shall be the Investment Manger hereunder only if the Bureau expressly consents in writing; and the resulting entity shall provide the Bureau with Part I and Part II of the Form ADV. The Investment Manger shall not hire or use subcontractors without prior written approval from the Bureau and any work subcontracted shall be at the expense of the Investment Manager.

11. Fees for Investment Management Services. The compensation of the Investment Manager for its services hereunder shall be calculated and paid quarterly in arrears by the Bureau in accordance with the attached Schedule B.

12. Representations. The Investment Manager represents that it is a bank, and insurance company, an investment management company or an investment advisor as defined by the Investment Advisers Act of 1940 will retain such status for the duration of this Agreement. The Investment Manager will promptly notify the Bureau in writing of any change or expected change in the status of the Investment Management company. The Investment Manager represents that it complies with all applicable federal, state, and local laws in the conduct of the work hereunder and represents that it will continue to do so for the duration of this Agreement. The Investment Manager accepts full responsibility for payments of all taxes and insurance including workers' compensation insurance premiums, unemployment compensation insurance premiums, all income tax deductions, social security deductions, and any and all other taxes or payroll deductions required for all employees engaged by it in the performance of the work authorized by this Agreement.

The Bureau warrants that it is a state agency statutorily created and deriving its authority from Ohio Revised Code Chapter 4121 and 4123. The Bureau represents that the appointment of the Investment Manager by the Bureau with respect to the investment of the assets allocated to the Investment Account, has been duly authorized by the Administrator pursuant to Ohio Revised Code

4121.121(B)(7), 4123.44 and The Ohio Bureau of Workers' Compensation Statement of Investment Policy and Guidelines. The Bureau further represents that the terms of this Agreement do no violate any obligations by which the Bureau is bound, whether arising by operation of rule or law.

13. Indemnification. The Investment Manger shall be liable for and shall indemnify the Bureau against any and all losses, damages, costs, expenses (including reasonable attorney fees), liabilities, claims and demands for any action, omission, information or recommendation in connection with the Agreement constituting a breach or violation of its fiduciary duties under applicable law, or a material breach of any agreement, representation, warranty or covenant made herein by the Investment Manager or its agents, except that the Investment Manger shall have no liability hereunder in the absence of negligence or reckless or willful misconduct on the part of itself or its agents. Subject to applicable law, the Investment Manager shall not be liable for any loss incurred in connection with the Investment Account due to bona fide (good faith) errors in judgment after having previously considered with due care the merits of any particular investment or investment strategy. If the Investment Manager makes any investment in violation of this Agreement and the guidelines set forth herein, such investment shall be sold and upon sale the following shall occur: (1) if such sale resulted in a

gain, the proceeds and any gain shall be credited to the Investment Account; or (2) if such sale resulted in a loss, the Investment Manager shall credit the Investment Account for the full amount of the loss.

14. Confidential Information. All information regarding operations and investments of the Bureau shall be regarded as confidential by the Investment in Manager and shall not be disclosed except as authorized in writing by the Bureau or otherwise required by law. Specifically, the Investment Manager and any person in its employ who has knowledge of the amount and kind of transactions entered into on behalf of the Bureau, shall not disclose the purpose or substance of the transaction while in progress. Upon completion of such transactions and the reporting of the completed transactions to the Bureau in the normal monthly reporting, the information may be disclosed as authorized in writing by the Bureau or as required by law.

15. Merger and Order of Priorities. It is mutually understood and expressly agreed that the provisions of the Bureau's Request for Proposals and the Investment Manager's response thereto are incorporated by references, and together with this Agreement, contain the entire agreement between the parties. The parties have entered into no agreements, express or implied, other than this Agreement. To the extent that any terms and

provisions of this writing conflict with and cannot be reconciled with the Request for Proposal or with the proposal submitted, the terms and provisions of this Agreement shall control.

16. Amendments, Modifications, Supplements and Headings. The parties may, by mutual agreement, amend, modify, supplement or rescind the terms of this Agreement. The term "this Agreement" shall be deemed to include any such future amendments, modifications, and supplements. Any such amendment, modification, supplement or rescission shall not be effective unless expressed in writing and signed by the parties hereto. The headings in this Agreement are for convenience only and are not intended to be part of, or to affect the interpretation of, the terms of this Agreement.

17. Termination. This Agreement may be terminated without any penalty at any time by either party upon thirty (30) days written notice. The Bureau may terminate this Agreement immediately upon breach or default by the investment Manager of any terms of this Agreement, any terms of the Request for Proposal, and any terms of the Investment Manger's response thereto, unless in the event of a breach that is subject to cure, the Investment Manger has cured such breach to the Bureau's satisfaction within fifteen (15) days from date notice of the breach was given by the Bureau.

In the event the Bureau exercises its right to terminate this Agreement, the Investment Manager shall not be relieved of any liability for damages sustained by the Bureau by virtue of any breach by the Investment Manger to the extent of remuneration paid and payable pursuant to this Agreement. The Bureau shall not be liable for any further claims, and the claims submitted by the Investment Manager shall not exceed the total amount of consideration stated in this Agreement. The Bureau may withhold payment due to the investment Manager pursuant to this Agreement or otherwise, for the purpose of set-off until such time as damages due to the Bureau are determined. The Investment Manager, upon receipt of notice of termination is permitted to complete transactions in progress but shall cease commencing any new transactions and take all necessary or appropriate steps to minimize costs, and furnish a report, as of the date of receipt of notice of termination describing the status of all transactions pursuant to this Agreement, as the Bureau may require. In the event of termination of this Agreement, any documentation in the form of reports and analysis provided by the Investment Manager which fulfills any obligation of this Agreement shall be considered the property of the Bureau with the exception of any copyrighted notes, software developed by the Investment Manager to be used in the course of the Investment Manager daily operations to monitor and assist in the management of client accounts and other generic

documents prepared for distribution to Investment Manager's clients for general informational purposes.

The rights of termination referred to in this Agreement are not intended to be exclusive and are in addition to any other rights and remedies available to either party at law or in equity.

18. Default By The Investment Manager. The Bureau declares and the Investment Manager acknowledges that a default shall occur in the event in Investment Manager does not perform in accordance with the performance measures identified in the Statement of Investment Policy and Guidelines, or under-performs when compared to comparable managers in the particular sector as identified in the Performance Standards Section of Schedule A and the Bureau may terminate the Agreement. The Bureau declares and the Investment Manager acknowledges that a default shall occur in the event there is a change in the firm structure, including a change in the investment focus or a material change in personnel in the Bureau may terminate the Agreement. The Bureau declares and the Investment Manager acknowledges that a default shall occur in the event the Investment Manger becomes subject to regulatory or legal proceedings which the Bureau judges to be injurious to the Bureau or to its fiduciary duties, and the Bureau may terminate the Agreement.

19. No Additional Waiver implied. If the Investment Manager fails to perform an obligation or obligations under the Agreement or otherwise is in default and thereafter such failure or default is waived by the Bureau, such waiver shall be limited to the particular failure are default so waived and shall not be deemed to waive other failure or default hereunder. Waiver by the Bureau shall not be effective unless it is in writing.

20. Governing Law - Severability. The validity, construction and performance of the Agreement and the legal relations among the parties to the Agreement, shall be governed by and construed in accordance with the laws of the State of Ohio. If any provision of the Agreement of the application of any such provision shall be held by a court of competent jurisdiction to be contrary to law, the remaining provisions of the Agreement shall remain in full force and effect. The parties agree to submit irrevocably to the jurisdiction of Ohio courts.

21. Publicity. Any use or reference to this Agreement by the Investment Manager to promote, solicit, or disseminate information regarding the scope of the Agreement is prohibited, unless otherwise agreed to in writing by the Bureau. The Bureau agrees to be used as a reference by the Investment Manager in other State of Ohio competitive bidding situations.

22. Conditions Precedent. It is expressly understood by the parties any resulting Agreement is not binding on the Bureau until such time as all necessary funds are made available and forthcoming from the appropriate state agencies, and when required, such expenditure of funds is approved by the Bureau.

23. Nondiscrimination. The hiring of employees for the performance of work under this Agreement shall be done in accordance with Ohio Revised Code Sections 153.59 and 153.591, and the Governor's Executive Order of January 27, 1972 and the Govern's amended Executive Order 84-9 of November 30, 1984. The Investment Manager shall not discriminate against or intimidate any person hired for the performance of the work by reason of race, color, religion, national origin, ancestry, sex, handicap, or disability, as such term is defined in the Americans with Disabilities Act. For any violation, the Investment Manager shall suffer such penalties as provided for in the Ohio Revised Code Section 153.60 and the Governor's Executive Order of January 27, 1972, or otherwise provided by law.

24. Drug-Free Workplace. The Investment Manager agrees to comply with all applicable state and federal laws regarding drug-free workplace. Investment Manage shall make a good faith effort to ensure that all its employees, if working on state property, will not purchase, use or possess illegal

drugs or alcohol or abuse prescription drugs in any way.

25. Time of Performance. The Agreement shall be binding upon both parties upon receipt by the Investment Manager of a copy of a fully executed agreement and compliance with any and all conditions precedent, except the services may commence on such later date as the Bureau may establish by written notification to the Investment Manager. The Bureau acknowledges receipt of the Investment Manager's ADV form, Part II, as currently filed, at least forty-eight (48) hours prior to entering into this Agreement.

26. Notification. All notices, instructions or report required or permitted under this Agreement shall be deemed to have been properly given if sent by regular U.S. Mail, first class postage prepaid, addressed as follows:

As to the Bureau:

Robert G. Cowman
Chief Investment Officer
30 West Spring Street, L 27
Columbus, Ohio 43215-2258

As to the Investment Manager:

Mark D. Lay
MDL Capital Management, Inc.

225 Ross Street, Third Floor
Pittsburgh, Pennsylvania 15219

27. Food and Beverage. Investment Manager shall provide necessary food and beverages at or associated with training or information sessions provided or conducted by the Investment Manager with the Oversight Commission or staff held outside of Columbus, Ohio.

28. Year 2000 Compliance. Investment Manager guarantees that all services provided under this Agreement will be "year 200 compliant" by December 1998, meaning that all services are designed to operate without regard to the turning of the century and that any process involved in these services which involves dates will operate in a manner that takes into account dates occurring before and after the turning of the century and that any process involved in these services creates, processes and stores dates in a format that accurately reflects whether the date is before or after the year 2000.

Proof of compliance shall be sent to the Bureau and shall indicate the date of implementation and describe in detail the upgraded software used in managing the funds and any necessary upgrades to the firewalls and operating systems. Failure to make adequate assurance by the above listed date shall be deemed a breach and shall terminate this Agreement. The provisions of this

paragraph shall survive any termination or expiration of this Agreement.

IN WITNESS WHEREOF, the parties hereunto affix their signatures this 14th day of May 1998.

MDL CAPITAL MANAGEMENT, INC.
TAX ID# : 25-1700296
S/ Mark D. Lay
Name: Mark D. Lay
Title: Chairman & CEO

STATE OF OHIO, BUREAU OF WORKER' COMPENSATION
TAX ID # 31-1334167
S/ James Conrad
James Conrad
Administrator

SCHEDULE A TO
INVESTMENT MANAGEMENT AGREEMENT

Client: State of Ohio, Bureau of Workers' Compensation
Investment Manager: MDL Capital Management

INVESTMENT GUIDELINES
Active Duration Fixed Income Management

Statement of Purpose
The purpose of these guidelines is to:

- establish the investment objective and performance standards of the Investment Account,
- ensure the investment Manager has the capability evaluate the risk of the financial instruments in which the Investment Account is vested, and
- prevent Investment Manager from exposing the Investment Account to excessive overall levels if risk exposure to inappropriate risk sources, or disproportionate exposure to any one risk source.

Investment Objective
The basic objective is to attain the highest total return consistent with a reasonable degree of risk by investing in fixed income securities. Success in achieving that objective will be measure by comparing the risk adjusted return and the after-

fee return of the Investment Account to the Lehman Brother Aggregated Bond Index.

Investment Guidelines

Investment Manager will manage a high quality, diversified fixed income Investment Account consistent with the Investment Account objectives outlined above in compliance with the Guidelines state below. Investment Manager will have full discretion to manage this Investment Account subject to Chapter 4123 of the Ohio Revised Code, the Bureau's Investment Policy, and the maturity credit diversification and marketability guidelines contained herein.

Eligible Securities

- Securities issued by U.S. corporations where both principal and interest are denominated and payable in U.S. dollars are permitted.
- With the exception of U.S. Treasury, Agency and Instrumentality securities, the maximum allocation of Investment Account market value to all classes of securities of any one issuer is 5% at the time of purchase (3% for entities with securities rated below A)
- Custodial Agent's STIF account and commercial paper rated at least A-1 or P-1 are permitted up to 10% of the market value of the Investment Account at the time of purchase. Repurchase agreements are permitted, provided that the collateral is delivered into the Investment Account, and

that the collateral would otherwise be eligible for direct purchase under these guidelines.

- Mortgage dollar rolls are permitted as long as there is sufficient case equivalents and short duration (under one year) securities in the Investment Account to offset the purchase cost of the rolls. No leverage permitted.
- Agency and non-agency mortgage securities are limited to pass-through securities, sequentials, CMOs, PACs, Ios, ARMs, CMBSs and multifamily securities.
- 144A securities are eligible as long as they have registration rights.
- Use of convertible bonds, convertible preferred stocks and preferred stocks are not permitted except for securities such as bank trust preferreds which have a stated final maturity date.

Prohibited Securities

- Dollar denominated foreign debt securities such as Yankees and Brady Bonds are prohibited.
- Securities denominated in currencies other than the U.S. dollar (non-dollar bonds) are prohibited.
- Private placement are prohibited except for 144A securities with registration.
- High yield securities are prohibited

- Use of inverse floaters, other exotic derivatives and reverse repurchase agreement is prohibited.
- 144A securities without registration rights are prohibited.
- Use of Eurodollar futures and options is prohibited.
- Use of listed U.S. fixed income futures and options contracts is prohibited.

Credit Quality

- The overall average Investment Account quality will be maintained at A or higher, as defined by Standard & Poor's. The minimum quality per security is BBB at the time of purchase by Standard & Poor's, Moody's, Duff & Phelps, or Fitch. In the case of split rated securities, the lowest rating will be used to determine eligibility.

Duration Range

- In no case, will the Investment Account's effective duration be outside of 50% corridor around the benchmark's effective duration (i.e. with 50% - 150% of benchmark's effective durations).

Designated Benchmark

Performance results will be monitored and evaluated on a quarterly basis against the Lehman Brothers Aggregated Bond Index.

Performance Standards
The value-added performance objective above the stated benchmark is outline below:

Benchmark	**Value-Added Per Annum**
Lehman Brothers Aggregated Bond Index	75

Time Horizon
3 and 5 year
rolling periods

The secondary performance objective of this Investment Account will be to place above the median manager of Callan's Active Duration Style Group or other institutionally managed active duration fixed income accounts over rolling 3 and 5 year periods as designated by the Bureau. The Investment Manger will be provided with all necessary analytics to understand and monitor this benchmark.

Personnel/Style
Continuity in personnel is vitally important to a successful investment management program. It is understood that any changes in key personnel, investment management philosophy, style, or approach, and significant changes in ownership affiliations, organizational structure, financial condition or clientele will be discussed in detail with the Bureau's Chief Investment Officer.

Additional and Withdrawals from the Investment Account

The Bureau may at any time make additions to and withdrawals from the Investment Account in such amounts as the Bureau shall deem appropriate, provided that all withdrawals and additions shall be made after giving the Investment Manager timely notices. Notice of withdrawals shall be considered timely if communicated to the Investment Manager no less than 10 business days prior to the withdrawal date. Notice of additions shall be considered timely if communicated to the Investment Manager no less than two business days prior to the date of deposit. The Investment Manager will notify the Bureau immediately if they are unable to comply with the withdrawal request or notice of addition to the Investment Account.

Data Requirements and Reports

The Investment Manager will provide monthly reports on the Investment Account to the Chief Investment Officer of the Bureau. These reports shall include a summary of Investment Account holds, transactions, performance, compliance with the Bureau Guidelines, and analytics on diversification and risk measures. The performance and holding information is to be delivered no later than two weeks after the end of the month.

In addition to the monthly reporting required above, the Investment Manager will send the Bureau a quarterly report which list the dollar

amount of transactions done with each broker used for the Bureau's transactions. This report should separate the brokers and give subtotals for the Ohio qualified broker, minority brokers, and national brokers. The quarterly report should also detail any soft dollar services received for Bureau transactions; and any commission recapture arrangements should be disclosed. The quarterly reports are to be delivered no later than three weeks after the end of the month.

The Investment Manager will also provide any other reports reasonably requested by the Bureau. These reports are to be provided to the Bureau and other recipients as directed by the Bureau.

Meetings

Performance review and investment strategy meetings will be held on a semi-annual basis.

Fiduciary Responsibility

The Investment Manager accepts full responsibility for the Bureau's assets under its management under the Ohio Revised Code and any applicable federal and state law.

Investment Policy Amendments

If any item, guideline or constraint within these Investment Guidelines proves to be too restrictive in practice, it will be the Investment Manager's responsibility to prepare a modification and/or amendment to that specific item in writing for

consideration by the Bureau's Chief Investment Officer.

Access to Records
The Bureau and the Bureau's auditors will have reasonable access to Investment Manager's records during normal business hours upon reasonable prior notice.

Conflict of Interest
Investment activities should be conducted in manner consistent with the Code of Ethics and the Standards of Professional Conduct adopted by the Association of Investment Management and Research.

SCHEDULE B TO INVESTMENT MANAGEMENT AGREEMENT

Client: State of Ohio, Bureau of Workers' Compensation
Investment Manager: MDL Capital Management, Inc.

INVESTMENT MANAGEMENT FEE

For Investment management services provided, the Bureau will pay Investment Manager an annual fee in accordance with the following based on the Investment Account Average Assets. Such fee shall be paid quarterly in arrears upon invoice and prorated on a daily basis for any quarterly period

during which the Agreement is in effect for only a portion of the quarter. Average Assets shall be determined by computing the market value Investment Account assets on the last business day of the calendar quarter. The market value of the Investment Account assets shall be based on the reports supplied by the Bureau.

Annual Fee

.30% on the first $25 million
.25% on the next $50 million
.20% on the next $100 million

This purely asset-based fee schedule shall not exceed any purely asset-based fee schedule of the investment Manager's other discretionary accounts: (a) managed in accordance with substantially identical investment guidelines and objectives; (b)of comparable size; and © of clients which became clients of the Investment Manager after May1, 1998.

SCHEDULE C TO
INVESTMENT MANAGEMENT AGREEMENT

Client: State of Ohio, Bureau of Workers' Compensation
Investment Manager: MDL Capital Management, Inc.

TRANSACTION PROCEDURE

The Investment Manager will have full discretion, subject to the Guidelines of the Investment Manager Agreement and Schedules and the Bureau's Investment Policy, when making security transactions. When the Investment Manager executes a sale transaction, it will notify the Bureau's designated Security Lending Agent. Upon execution of any transaction (purchase or sell) the Investment Manager will complete a trade ticket which will include information regarding the Approved Broker, the dollar amount, the security description, the trade/settlement dates, and special delivery instructions. Each trade ticket will be faxed to the Bureau's Investment Department no later than Trade Date plus one day. In addition, the Investment Manager will inform the Bureau's Investment Department by phone of each fax sent regarding a transaction. The Investment Manager will inform the Approved Broker to enter all transactions to the DTC ID system or other electronic system, whether the security is eligible for DTC settlement or not. The Investment Manager will receive detailed settlement instructions from the Bureau. If confirmation is not available on the DTC system, the Investment Manager will require the broker to send a confirm to the Bureau. The Bureau will affirm all transactions with DTC once trade information has been verified by the Investment Manager. The settlement of all transactions will be the responsibility of the Bureau's

Custodian who will contact the Bureau's Investment Department who will then notify the Investment Manager. It will be the Investment Manager's responsibility to correct all fails caused by the broker selected by the Manager. Fails caused by the Bureau's Custodian will be corrected by the Bureau.

Proceeds Received from sales, expenditures made for purchase, and income earned on the assets in the Investment Account will be charged to or deposited in the Investment Manager's account with the Bureau's Custodian. The Bureau will manage the cash in the Investment Manager's Custodial Account. Currently the only investment vehicle available for the investment of cash is the Custodian's STIF account. It is the Investment Manager's responsibility to ensure there are enough cash equivalents or sale proceeds to cover purchases made by the Investment Manager. It will be the responsibility of the Investment Manager to ensure that no overdraft occurs in the Investment Manager's Custodial Account. However, should the Investment Manager overdraw the Custodial Account, the Investment Manager will, at it's own expense, remedy the overdraft as soon as possible.

INVESTMENT ADVISORY AGREEMENT

THIS INVESTMENT ADVISORY AGREEMENT ("Agreement"), made as of the 18th day of November, 2002, between **MDL ACTIVE DURATION FUND, LTD.**, an excepted company incorporated under the laws of Bermuda (the "Company"), and **MDL CAPITAL MANAGEMENT, INC.** a Pennsylvania corporation (the "Investment Adviser").

RECITALS

A. The Company was incorporated in Bermuda on May 20, 2002 as an investment vehicle through which United States tax exempt investors and non-United States resident investors can invest in a portfolio consisting primarily of government, corporate and mortgage-backed fixed income securities as more fully described in the Company's Confidential Private Placement Memorandum dated December 2, 2002, as the same may be amended, restated or supplemented from time to time (the "Memorandum").

B. The Company desires to retain the Investment Adviser, which is an investment adviser registered under the Investment Advisers Act of 1940, as amended (the "Advisers Act") as the investment adviser for the Fund.

C. The Investment Adviser desires to accept such retainer upon the terms and conditions set forth herein.

D. Capitalized terms not otherwise defined in this Agreement shall have the meanings ascribed to them in the Memorandum.

NOW, THEREFORE, the Company and the Investment Adviser do mutually promise and agree as follows:

1. **Investment Advisory Services**. The Company hereby employs the Investment Advisor to manage the investment and reinvestment of the assets of the Company and to administer its business and administrative operations, subject to the discretion of the Board of Directors of the Company (the "Board of Directors"), for the period and on the terms set forth in this Agreement. The Investment Adviser herebty accepts such employment for the compensation herein provided and agrees during such period to render the services and to assume the obligation herein set forth.

2. **Authority of the Investment Advisor**. The Investment Advisor shall for all purposes herein be deemed to be an independent contractor and shall, unless otherwise expressly provided or authorized, have no authority to act for or represent the Company or the Fund in any way or

otherwise be deemed an agent of the Company or the Fund. However, one or more shareholders, officers, directors or employees of the Investment Advisor may serve as directors and/or officers of the Company, but without compensation or reimbursement of expenses for such services from the Company. Nothing herein contained shall be deemed to require the Company to take any action contrary to its Memorandum of Associates or Bye-Laws, as amended, restated or supplemented, or any applicable statute or regulation, or to relieve or deprive the Board of Directors of its responsibility and control of the affairs of the Company.

3. **Obligations of and Services to be Provided by the Investment Adviser**. The Investment Adviser undertakes to provide the services hereinafter set forth and to assume the following obligations;

(A) Management and Administrative Services

(1) The Investment Adviser, at its own expense and without reimbursement from the Company, shall furnish adequate office space , which may be space within the offices of the Investment Adviser or in such other place as may be agreed upon from time to time, and all office facilities and equipment as may be reasonably required for performing services relating to to

advisory, research, asset allocation, portfolio manager selection and evaluation activities and otherwise managing and administering investments of the Company.

(2) The Investment Adviser shall employ or provide and compensate the executive, administrative, secretarial and clerical personnel necessary to supervise the provision of the services set forth in sub-paragraph 3(A)(1)and shall bear the expense of providing such services, except as provided in Section 4 of this Agreement. The Investment Adviser shall also compensate all directors, officers and employees of the Company who are directors, officers or employees of the Investment Adviser or its affiliated companies.

(B) Investment Advisory Services

(1) The Investment Adviser shall, subject to and in accordance with the Investment Policy of the Company as set forth in the Memorandum and any directions which the Board of Directors may issue to the Investment Adviser, have overall responsibility and discretion for the general management and investment of the assts and securities portfolios of the Company, including without limitations selecting and evaluating investment of the Company's assets and investing through the Master Fund.

(2) The Investment Adviser shall develop overall investment programs and strategies for the company consistent with the Investment Policy, shall revise such programs as necessary, and shall monitor and report periodically to the Board of Directors concerning the implementation of the programs.

(3) Subject to the supervision of the Company's Board of Directors and at all times in accordance with the Investment Policy as set forth in the Memorandum, the Investment Adviser is authorized to:

(a) effect purchase, sales and other transactions using the assets of the Company.

(b) direct custodians to deliver funds or securities for the purpose of effecting transactions, and to instruct custodians to exercise or abstain from exercising any privilege or right attaching to such assets;

(c) make all decisions relating to the manner, method and timing of investment transactions, and to select brokers and dealers for the execution, clearance and settlement of any transactions;

(d) enter into, make and perform all contracts, agreements and other undertakings as may in the opinion of the Investment Adviser be

necessary or advisable or incidental to the carrying out of the objectives of this Agreement including an administrative services agreement, custodian agreement and others;

(e) trade on margin, to borrow from banks, brokers or other financial institutions and to pledge assets of the Company in connection therewith;

(f) retain consultants or other service providers to the Company; and

(g) make and execute, in the name and on behalf of the Company, all such documents (including, without limitation, customer agreements and other documents in connection with the establishment and maintenance of brokerage accounts) and to take all such other actions which the Investment Adviser considers necessary or advisable to carry out its investment management duties hereunder. With regard to any documents or agreements executed in the Company' s name, copies will be promptly provided to the Company and the Administrator so as to advise the Company and the Administrator of the existence of such documents and agreements and apprise them of any obligations thereunder.

(4) The Investment Adviser shall render to the Board of Directors such periodic reports concerning the business and investments of the Fund as the Board of Directors shall reasonably request.

(5) The Investment Adviser shall take such appropriate actions and maintain such procedures as are reasonably necessary to ensure that assets of the Company ar not purchade from or sold to a "party in interest" as the term is defined in the Employment Retirement Income Security Act of 1974, as amended ("ERISA") other than as may be permissible pursuant to any applicable provisions of ERISA or appropriate prohibited transaction exemptions of the United States Department of Labor (the "DOL").

In exercising its rights and carrying out its duties hereunder, the Investment Adviser is authorized to act for the Company and on the Company's behalf within the scope of this Agreement either itself or wholly or in part through its authorized dealers or delegates in the same manner and with the same force and effect as the Company might or could do.

(C) Provision of Information Necessary for Preparation of Securities Registration Statements, Amendments and Other Materials. The Investment Adviser will make available and provide financial, accounting and statistical information required by the Company for the preparation of filings, reports and other documents required by federal and state securities laws, and with such information as the Company may reasonably request for use in the preparation of such documents or of other

materials necessary or helpful for the offering and sale of the Company's shares.

(D) Provisions of Personnel. The Investment Adviser shall make available its offices and employees to the Board of directors of the Company for consultation and discussions regarding the administration and management of the Company and its investment activities.

4. **Expenses**. The Investment Adviser shall not be required to pay any expenses of the Company except as provided herein. The expense of the Fund's operations borne by the Company include by way of illustration and not limitation, director and officer liability insurance, reports to shareholders, reports to government authorities, interest charges, reimbursement payments to securities lenders for dividend and interest payments on securities sold short, taxes, legal expenses, auditing and accounting services, insurance premiums, brokerage and other expenses connected with the execution of portfolio securities transactions, fees and expenses of dividend disbursing agents, registrars and stock transfer agents and the cost of keeping all necessary shareholder records and accounts.

5. **Compensation of the Investment Adviser**.

(A) Management Fee. For services and facilities to be rendered and the charges and

expenses to be assumed by the Investment Adviser hereunder, the Company shall pay to the Investment Adviser a management fee, accrued monthly and paid quarterly ("Management Fee"). The Management Fee shall be calculated at an annual rate of 1% of the net assets of the Fund as of the last Business Day of each calendar month. For any month in which this Agreement is not in effect for the entire month, such fee shall be reduced proportionately on the basis of the number of calendar days during which it is in effect and the fee computed upon the net assets on the last Business Day during which it is so in effect. The Investment Adviser may, in its sole discretion, effectively waive all or any part of the Management Fee due with respect to any shareholder's investment, by rebate or otherwise.

(B) Incentive Fee. The Investment Adviser is also entitled to receive a quarterly performance-based fee from the Company, calculated on a Series-by-Series basis, in an amount equal to 20% of the appreciation of each Series' Net Asset Value with respect to a particular calendar quarter in excess of the Hurdle (as defined herein) for that quarter (the "Incentive Fee"). The Hurdle with respect to a calendar quarter means an amount equal to the opening Nett Asset Value of the relevant Series for such calculation period multiplied by a percentage based on the return of the Lehman Brother Government Credit Bond Index for the calculation period (the"Hurdle"). The

Hurdle return will be prorated for any calculation period of less than a calendar quarter. The Incentive Fee is calculated on a Series-by-Series basis in an effort to ensure that Incentive Fees are equitably assessed among shareholders. The Incentive Fee, if any is calculated and payable (i) as of the last Business Day of each calendar quarter, (ii) as of each Redemption Date with respect to the Shares redeemed by redeeming shareholders, (iii) in the Company's sole discretion, as of the effective date of transfer of Shares, and (iv) as of the date of termination of this Agreement, in each case with respect to the period then ending. All fees and expenses (except the Incentive Fee) that have been accrued or paid (but not previously accrued) for a given period are deducted prior to calculating the Incentive Fees for such period, including, without limitation, the Management Fee. Appropriate adjustments are to be made to account for subscriptions and redemptions. The Investment Adviser, in its sole discretion, may effectively waive all or part of its Incentive Fee otherwise due with respect to any shareholder's investment, by rebate or otherwise.

(C) High Water Mark. The Incentive Fee with respect to a Series of Shares is calculated on a cumulative basis and is payable only where the Net Asset Value per Share of that Series has risen above (i) the higher of the issue price of the Shares in the relevant Series or, (ii) the Net Asset Value per share of the relevant Series immediately following

the last calculation of an Incentive Fee with respect to such Series plus the amount of the Hurdle for such period and net of the Incentive Fees calculated abd payable at such time. In effect, the Incentive Fee payable with respect to a Series is not payable until all prior net losses with respect to such Series (including the cumulative Hurdle amount and excluding the Incentive Fee from the calculation of net losses) are recouped. Appropriate adjustments shall be made to account for subscriptions and redemptions.

(D) Deferral. Notwithstanding the foregoing, the Investment Adviser may elect prior to the commencement of the Company's trading activities with respect to its first year of trading and prior to the commencement of each calendar year thereafter, to defer for a period of up to ten years payment of all or any portion of its Management Fees and Incentive Fees earned with respect to that subscription period. In such case, the deferred amount will appreciate or depreciate based, at the election of the Investment Adviser, on either (i) the subsequent performance of the Fund (before Management and Incentive Fees), or (ii) the performance of any other investment chosen by the Investment Adviser prior to the commencement of the deferral period. An accounting of any such deferred fees and their investment performance shall be made at the end of each calendar year by the Company. Notwithstanding anything contained herein to the

contrary, the Company may enter into other deferred compensation arrangements with regard to the deferred Management and/or Incentive Fees including, without limitation, arrangements properly referred to as "rabbi trusts." Any deferred fees will not be charged a Management Fee or Incentive Fee. The deferred fees will be reflected on the books of the Company as a liability and will reduce the Company's Net Asset Value, but will not be treated as "leverage" for purposes of any leverage limitations imposed on the Company. On the date of expiration of the deferral period, dissolution of the Company or termination of the Agreement by the Company, all applicable deferred fees, if any, held by the Company on behalf of the Investment Adviser will be paid to the Investment Adviser. Upon termination of the Agreement by the Investment Adviser, fees elected to be deferred by it will remain in the Company until the earlier of the end of the deferral period or the dissolution of the Company.

(E) Payment of Management Fee and Incentive Fee. Both the Management Fee and the Incentive Fee are payable by the Company to the Investment Adviser within a reasonable time after each becomes due. Payment of the Incentive Fee, however, will be subject to adjustment upon completion of the audit of the Company's financial statements for the fiscal year in which the Incentive Fee accrues. If the Incentive Fee paid for a fiscal year was higher or lower than Incentive Fee that

actually was due, an appropriate adjustment will be made and payment will be made within a reasonable time after completion of the audit.

6. **Exclusivity; Services to Other Clients**. The Company acknowledges the Investment Adviser performs investment advisory services for various other clients and that the Investment Adviser may give advice and take action with respect to any of its other clients that differs from the advice given or timing or nature of action taken with respect to the Company. The Company further acknowledges that the Investment Adviser may from time to time invest the Company's assets in securities also purchased by other clients of the Investment Adviser. The Investment Adviser will, under normal conditions, allocate investment opportunities to the Company over a period of time on a fair and equitable basis relative to its other clients, subject to applicable laws. The Company acknowledges and agrees that the Investment Adviser shall not have any obligation to purchase or sell for the Company any securities that the Investment Adviser, its principals, affiliates or employees, may purchase or sell for their own accounts or for the account of any other client. In Certain circumstances, the Investment Adviser may from form other pooled investment vehicles, including the Master Fund, for the purpose of making investments or a particular investment and may cause the Company to invest in such investment vehicles. The Investment Adviser and other clients

of the Investment Adviser may also invest in such investment vehicles. Although the Investment Adviser has agreed to permit the Company to use the name "MDL", if it so desires, it is understood and agreed that the Investment Adviser reserves the right to use and to permit other persons, firms or corporations, including investment companies, to use such name.

7. **Exculpation and Indemnification**.

(A) Exculpation. In the absence of fraud, willful default, bad faith, gross negligence or reckless disregard of obligations or duties hereunder on the part of the Investment Adviser or any shareholder, agent, director, officer or affiliate thereof ("Investment Adviser Affiliates"), neither the Investment Adviser nor any the Investment Adviser Affiliate shall be subject to liability to the Company or to any shareholder of the Company for any act or omission in the course of, or connected with, rendering services hereunder, or for any losses that may be sustained in the purchase, holding or sale of any security, provided, however, that the limitation of liability contained in this Section 7(A) shall not apply to any liability, costs or expenses imposed on the Investment Adviser or any Investment Adviser Affiliate under ERISA.

(B) Indemnification. Except as otherwise required by law or the provisions of this Agreement, the Company shall indemnify, defend and hold harmless the Investment Adviser and each

Investment Adviser Affiliate (severally, an "Indemnified Person") from and against any losses, liabilities, damages, costs or expenses (including, without limitation, reasonable attorney fees and expenses in connection therewith and amounts paid in settlement thereof) to which any of such Indemnified Persons may directly or indirectly become subject, in connection with (a) any act or failure to act or any alleged act or failure to act arising out of, in connection with or related to the Company, or (b) the affairs of the Company, but only to the extent that such Indemnified Person (x) was neither grossly negligent nor engaged in fraud, bad faith or reckless disregard of obligations or duties hereunder, (y)did not willfully breach any material term or provision of this Agreement and (z) did not willfully violate any material law relating to the Company; provided, however, that the indemnification contained in this Section 7(B) shall not apply to any liabilities, costs or expenses imposed on the Investment Adviser or any other Indemnified Person under the Securities Act (to the extent such indemnification is determined to be contrary to public policy) or under ERISA. The Company shall pay the expenses incurred by any such Indemnified Person in connection with any proceeding in advance of the disposition of such matter by a court of competent jurisdiction upon receipt of a written undertaking by such Indemnified Person to repay the full amount advanced if there is a determination by any such

court that such Indemnified Person is not entitled to indemnification with respect thereto.

8. **Brokerage Commission**. The Investment Adviser, subject to the control and direction of the Board of Directors, shall have authority and discretion to select brokers and dealers to execute portfolio transactions for the Company and for the selection of the markets on or in which the transactions will be executed. The Investment Adviser may cause the Company to pay a broker-dealer which provides brokerage and research services, as such services are defined in Section 28(e) of the Securities Exchange Act of 1934 (the "Exchange Act"), to the Investment Adviser a commissions for effecting a securities transactions in excess of the amount another broker-dealer would have charged for effecting such transactions, if the Investment Adviser determines in good faith that such amount of commission is reasonable in relation to the value of brokerage and research services provided by the executing broker-dealer viewed in terms of either that particular transaction or its overall responsibilities with respect to the accounts as to which it exercises investment discretion (as defined in Section 3(a)(35) of the Exchange Act). The Investment Adviser shall provide such reports as the Board of Directors may reasonably request with respect to the Company's total brokerage.

9. **Representations and Acknowledgments of Investment Adviser**. The Investment Manager represents and warrants that it is an investment adviser as defined under the Advisers Act and is registered under the Advisers Act. The Investment Adviser also acknowledges that it is a fiduciary with respect to the Company and assumes the duties, responsibilities and obligations of a fiduciary under ERISA. The Investment Adviser further represents and warrants that:

(A) The Investment Adviser complies with the bonding requirements of Section 412 of ERISA and satisfies similar bonding requirements under state or Federal law.

(B) The Investment Adviser has complied and will continue to comply with all regulations, registrations, filings, approvals, authorizations, consents or examinations required by the United States Securities and Exchange Commission, the DOL, or any other governmental authority having jurisdiction over the activities contemplated by this Agreement.

U.S. Department of Justice
Office of the Solicitor General

Acting Solicitor General Washington, D.C. 20530

December 23, 2010

Percy Squire, Esq.
Percy Squire, Co., LLC
514 S. High Street
Columbus, Ohio 43215

Re: Mark D. Lay v. United States,
S. Ct. No. 10-695

Dear Mr. Squire:

As requested in your letter December 20, 2010, I hereby consent to the filing of amicus curiae brief in the above-captioned case on behalf of Samuel S. Paschall, Eric Carmichael, Gerald Sherwin, Orin Grimes, National Association of Investment Companies, Pascal Nardelli, Charles Zappala, Tracy Foster, Leroy Thomspon, Chuck Sanders, Bruce T. Goode, James C. Roddey, Joe Orlando, James Hardiman, Bobby Law, and Claude Anderson.

Due to continuing delay in receiving incoming mail at the Department of Justice, in addition to mailing your brief via first class mail, we

would appreciate a fax or e-mail copy of your brief. If that is acceptable to you, please fax your brief to Emily C. Spadoni, Supervisor Case Management, Office of the Solicitor General at (202) 514-8844, or email at SupremeCtBriefs@USDOJ.gov. Ms. Spadoni's direct dial phone number is (202) 514-2217 or 2218.

Very truly yours,
S/ Neal Kumar Katyal
Neal Kumar Katyal
Acting Solicitor General

184 (6)

№. 10-695

Supreme Court, U.S
FILED
MAR 25 2011
OFFICE OF THE CLERK

In The
Supreme Court of the United States

MARK D. LAY,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

CORRECTED PETITION FOR REHEARING

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Columbus, OH 43215

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April, 2011

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TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

ARGUMENT 1

CONCLUSION 27

TABLE OF AUTHORITIES

CASES

Cleveland v. United States,
531 U.S. 12 (2000) 4

Goldstein v. SEC,
451 F.3d 873 (D.C. Cir. 2006) . . . 13, 14, 16

Rewis v. United States,
401 U.S. 808 (1971) 9

Skilling v. United States,
561 U.S. _____ (2010),
130 S. ct. 2896 2010 U.S.
LEXIS 5259 (June 24, 2010) . . . . . *passim*

United States v. Grossman,
843 F. 2d 78 (2d Cir. 1988) 3, 4

United States v. Lane,
474 U.S. 438 (1986) 2

United States v. Males,
459 F. 3d 154 (2d Cir. 2006) 4

United States v. Marando,
504 F.2d 126(2d Cir. 1974) 3, 4

United States v. Maze,
414 U.S. 395 (1974) 4

United States v. Pimental,
236 F. Supp. 2d 99 (D.C. Mass 2002) . . . 6, 7

United States v. Prince,
214 F. 3d 740 (6th Cir. 2000) 1

United States v. Smith,
419 F.3d 521 (6th Cir. 2005) 25

United States v. Tines,
70 F.3d 891 (6th Cir. 1995) 25

STATUTES

18 U.S.C. §1341 . . . . . *passim*

ARGUMENT

Reconsideration of the denial of certiorari is requested for the reason, the following key issues are not addressed in the denial: 1) the impact of trade confirmation slips; 2) the fact the Mr. Lay did not receive fees from the Ohio Bureau of Workers' Compensation for his investment adviser work on behalf of the Active Duration Fund (ADF); and 3) Mr. Lay did not realize gain from the alleged misconduct that formed the basis for his prosecution.

As was correctly pointed out in the dissent in the appellate court opinion in this action, in order to sustain a mail fraud conviction against Mr. Lay, the government was required to show proof of interstate mailing "in furtherance of the [alleged] scheme to defraud[.]" United States v. Prince, 214 F. 3d 740, 748 (6th Cir. 2000); see also, 18 U.S.C. §1341 (a mailing must be "for the purpose of executing such scheme or artifice" to defraud).

Here the charged mailings are "trade confirmation slips." The government did not contend and the evidence did not show that the slips themselves contained any misrepresentations or that they played any role whatever in parting the Ohio Bureau of Workers Compensation (OBWC) from its

money. Instead, the slips simply confirmed trades that Mr. Lay made on the open market.

The dissent correctly points out that the Governments' explanation of this point is amorphous at best. Post-fraud mailings, such as trade confirmations, can further a scheme if designed to lull the victims into a false sense of security, postpone their ultimate complaint to the authorities, and therefore make the apprehension of the defendants less likely than if no mailings had taken place. United States v. Lane, 474 U.S. 438, 451 (1986). Here, there was no proof to support such a theory. In Mr. Lay's case, all of the trades were done correctly, which the government did not contest. The government alleged that the trade confirmations were used in a scheme to over leverage the Active Duration Hedge Fund (ADF). The evidence at trial however did not show how any of the trades accomplished over leveraging. The fact is many trades reduced leverage, and many trades were profitable. The government never distinguished this fact. The evidence did not address individual trades or the dates of the trades. Without showing the daily position of the fund and any losses generated by the trades, the confirmation slips in and of themselves did not advance the government's case.

The trade confirmation statements did not contain false information. In cases where mailing trade confirmation statements constituted a violation of 18 U.S.C. §1341, the statements were transmitted for the purposes of executing the artifice of scheme. See, United States v. Marando, 504 F.2d 126(2d Cir. 1974) where trade confirmation slips were mailed and determined to be an integral part of a scheme to obtain property; also see, United States v. Grossman, 843 F. 2d 78 (2d Cir. 1988) where it was determined that:

> The mailings of the confirmation slips did further the purpose of executing the scheme. The confirmation slips (1) notified the relatives that the purchase or sale actually had been completed; (2) provided an on-going tally of purchases, allowing the relatives to cover each other's positions; (3) concealed the fraud by maintaining an appearance of normality, see, United States v. Cohen, 518 F.2d 727, 737 (2 Cir), cert denied, 423 U.S. 926, 46 L. Ed. 2d 252 (1975): and (4) allowed the relatives to demonstrate ownership after the recapitalization announcement. Pereira v. United States, 346 U.S. 1, 98 L. Ed. 435, 74 S. Ct. 358 (1954). [**27].

To establish a violation of the mail fraud statute, "the mailing must be for the purposes of executing the scheme." United States v. Maze, 414 U.S. 395 (1974). To state an offense under 18 U.S.C. §1341 this Court determined in Cleveland v. United States, 531 U.S. 12 (2000) that the evidence must show that the defendant not only devised scheme or artifice, but also used that scheme or artifice to obtain money or property. See, United States v. Males, 459 F. 3d 154 (2d Cir. 2006) (Emphasis added). Here the evidence showed ADF received its first $100,000,000.00 before Mr. Lay ever executed a trade. There was no evidence that the mail was used to obtain money or property. There was no evidence that property or money was obtained through a scheme that involved the use of the mail. The trade confirmation slips here unlike those in Grossman or Mirando did not contain false information, did not document illegal insider trades, and were not transmitted to obtain money or property. The alleged nondisclosures and misrepresentations concerning leverage alleged by the government were not related to the mailing of confirmation slips. The trades reflected on the listed slips were lawful trades for a hedge fund. It does not matter that OBWC did not authorize them, the relevant private placement

memorandum gave ADF's board sole discretion to deviate from the fund's leverage guideline, not OBWC. The trade confirmation statements report the purchases of securities on a certain date, from a certain broker, at a certain price. All of that information was true, in every instance. On these facts a violation of 18 U.S.C. §1341 was not established.

Here OBWC invested funds in ADF on three discrete dates, August 20, 2003, May 21, 2004 and September 23, 2004. These are the only times OBWC "parted" with property.

> The mail fraud statute prohibits the use of the mails by any person "having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises..." 18 U.S.C. §1341. "Mail fraud consists of (1) a scheme or artifice to defraud; (2) use of mails in furtherance of the scheme; and (3) intent to deprive the victim of money or property." United States v. Turner, 465 F.3d 667, 680 (6th Cir. 2006). Materiality of falsehood is a requisite element of mail fraud. Neder v. United States, 527 U.S. 1, 25, 119 S. Ct. 1827, 144 L. Ed. 2d 35 (1999). The misrepresentation "must have

> the purpose of inducing [*7] the victim of fraud to part with the property or undertake some action that he would not otherwise do absent the misrepresentation or omission." United States v. Daniel, 329, F.3d 480, 487 (6th Cir. 2003). A misrepresentation "is material if it has a natural tendency to influence, or is capable of influencing, the decision of the decision-making body to which it was addressed." Neder, 527 U.S. at 16 (internal citation and quotation marks omitted).

McCauliff, supra.

There was no proof here that OBWC parted with property by reason of a material misrepresentation in a trade confirmation slip.

> The mail fraud statute "does not purport to reach all frauds, but only those limited instance in which the use of the mails is part of the execution of the fraud." Kann v. United States, 323 U.S. 88, 95, 89 L. Ed. 88, 65 S. Ct. 148 (1944). Accordingly, the government must show beyond a reasonable doubt that [defendant] caused the mailings listed in the indictment to be sent and that the mailings were in furtherance of the fraud.

United States v. Pimental, 236 F. Supp. 2d 99 (D.C. Mass 2002).

Here there was no proof of any mailings in further of a scheme to exceed leverage or that the OBWC parted with money due to mailing trade confirmation slips.

On June 24, 2010, the United States Supreme Court in Skilling v. United States, 561 U.S. _____ (2010), 130 S. ct. 2896 2010 U.S. LEXIS 5259 (June 24, 2010) announced a seismic shift in mail fraud prosecutions. The appellate court totally ignored the Skilling opinion. The Skilling opinion highlights what the government's burden of proof is in a prosecution under 28 U.S.C. §1341for mail fraud. Skilling makes is clear that an essential element is a mail fraud prosecution is evidence of some form of gain or enrichment to the defendant. Skilling states:

> Enacted in 1872, the original mail-fraud provision, the predecessor of the modern-day mail and wire fraud laws, proscribed, without further elaboration, use of the mails to advance 'any scheme or artifice to defraud.' See, McNally v. United States, 483 U.S. 350, 356 (1987). In 1909, Congress amended the statute to prohibit, as it does today, 'any scheme or artifice to

> defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises §1341 (emphasis added); see id. at 357-358. Emphasizing Congress disjunctive phrasing the Courts of Appeals, one after the other, interpreted the term "scheme or artifice to defraud" to include deprivations not only of money or property but also of intangible rights.

Id. at *80-81 (emphasis added).

Skilling goes on to discuss the elements of an honest service fraud claim versus other frauds. In Skilling the Court pointed out the requirement for symmetry in a standard mail fraud case, that is the victim's loss of money or property supplied the defendant's gain with one the mirror image of the other. Id. at *82.

In this case it is undisputed that Mr. Lay did not realize any gain as a result of an alleged misuse of the mails. The OBWC's losses were due to unsuccessful attempts by Mr. Lay to recoup losses through increased use of leverage. In some instances gains resulted from the use of increased leverage. In other instances losses occurred from its use. In no

instance, however, did Mr. Lay realize any money or property from the use of allegedly excessive leverage.

Likewise, Mr. Lay has received no compensation from OBWC by reason of trading activity or volume. All of Mr. Lay's fees were paid by the ADF, not the OBWC. Mr. Lay received no compensation from OBWC for ADF trades. The absence of any gain of any nature by the Defendant is also fatal to a mail fraud prosecution. Skilling emphasizes this point.

Skilling determined that a 28 U.S.C. §1346 prosecution requires as "offense conduct" evidence of either bribery or kickbacks and that the "ambit of criminal statutes should be resolved in favor of lenity." Id. at 100 (quoting Rewis v. United States, 401 U.S. 808, 812 (1971)). The "offense conduct" in Mr. Lay's case which was a 28 U.S.C. §1341 prosecution according to Skilling, must include an element of gain at the expense of a victim, here OBWC.

In this case the gain element is totally lacking. The District Court stated in of Mr. Lay's sentencing memorandum:

> Looking back in hindsight, as the Court can do, it seems obvious that he should have stopped following the investment strategy he had in place. But at the time,

no one had ever seen an instance in which rising bond process would not lead to a devaluation of existing bonds. But that is precisely what happened in this time frame. It was the first time in economic history of the United States that that occurred, and his strategy failed and because of the leverage, failed dramatically.

***

It seems apparent that the defendant had not lost any monies for any clients in the management of the MDL investments until the defendant began excessive over-leveraging with the ADF. It appears from his past experiences with Mellon Bank and PNC the it was not the first time defendant took great risks in the belief that he could recoup his losses. The Court notes that the defendant, born in 1963, actively pursued a good education and did not demonstrate criminal tendencies. The defendant has no criminal record. The defendant appears to have been a responsible father. <u>It does not appear to the Court that the defendant was motivated to gain more income by his management of the ADF</u>.

(Trial Court Doc. #181 p. 23) (emphasis added).

As the District Court indicated, there was no evidence whatsoever that the mails were used by Mr. Lay in any scheme to defraud another or to generate gain for Mr. Lay. Skilling makes it clear the absence of this element is fatal to a mail fraud prosecution. The mailing of trade confirmation slips by third parties that document specific transactions did not result in any gain or benefit to Mr. Lay.

Rehearing should also be granted for the reason the Opinion of the Court of Appeals fails to address the ongoing regulatory measures being taken by the Securities and Exchange Commission to clarify duties owed by investment advisers to private funds, such as the Active Duration Fund here.[1] All of the

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[1]The SEC has now proposed rules to implement certain provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act regarding investment advisers to private funds, such as hedge funds and private equity funds. The proposals would:

- Establish reporting requirements for private fund advisers that will be required by the Dodd-Frank Act to register under the Investment Advisers Act of 1940 and more limited reporting requirements for certain private fund advisers that will continue to be exempted from registration under the Advisers Act;
- Increase the scope of disclosure required of all registered investment advisers of Form

operative agreements that governed ADF, Petitioner's relationship to OBWC, and the limitation imposed by these agreements, including the restrictions of hedge fund investments to qualified or sophisticated investors, have been ignored.

Petitioner here received no compensation from the Ohio Bureau of Workers Compensation (OBWC) for services as the ADF Investment Adviser. The

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ADV;

- Clarify the exemptions from Advisers Act registration available to advisers to venture capital funds and private funds with less than $150 million in assets under management in the United States, and foreign private advisers; and
- Clarify the parameters of the prohibition from SEC registration applicable to "mid-sized" investment advisers with between $25 million and $100 million in assets under management.

Proposed Rule: Rules Implementing Amendments to the Investment Advisers Act of 1940, Release No. IA-3110 (November 19, 2010), available at http://sec.gov/rules/proposed/201/ia-3110.pdf (the "implementing release"); and Proposed Rule: Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers, Release No. IA-3111 (November 19, 2010), available at http://www.sec.gov/rules/proposed/2010/ia-3111.pdf (the "exemptions release").
(See, Sullivan & Cromwell, LLP, November 24, 2010 Newsletter)

express terms of the governing agreements, i.e. the PPM and investment adviser agreement ADF refute this. Furthermore, there was no evidence whatsoever in the form of checks or transfers of any nature to establish that any fees paid to Petitioner were paid by OBWC, all fees having instead been paid, in accordance with the ADF Private Placement Memorandum by the Fund Administrator, Olympia Capital.

The novel issues in this case support the need for further review. There is no other case known to Petitioner where it has been determined that a hedge fund investor may also be a hedge fund client.

As has been stated, the SEC Hedge Fund rule concerning who is a hedge fund client was overturned by the United States Court of Appeals for the District of Columbia Circuit in the appellate case of Goldstein v. SEC, 451, F.3d 873 (D.C. Cir. 2006). The Court states:

> "An investor in a private fund may benefit from the adviser's advice (or he may suffer from it) but he does not receive the advice directly. He invests a portion of his assets in the fund. The fund manager - the adviser - controls the disposition of the pool of capital in the fund. The adviser does not tell the investor how to spend his money;

> the investor made that decision when he invested in the fund. Having bought into the fund, the investor fades into the background; his role is completely passive. If the person or entity controlling the fund is not an "investment adviser" to each individual investor, the a fortiori each investor cannot be a "Client" of that person or entity."

Under Goldstein it is clear that investment advisers do not owe fiduciary duties to hedge fund investors for the reason the investors are not the advisers' clients and as such observing fiduciary duties to the investor instead of the fund would pose inevitably conflicts of interests.

In point of fact, Goldstein states:

> At best it is counterintuitive to characterize the investors in a hedge fund as the "clients" of the adviser. *See Am. Bar Ass'n v. FTC, c 368 U.S. App. D.C. 368, 430 F.3d 457, 471 (D.C. Cir. 2005).* The adviser owes fiduciary duties only to the fund, not to the fund's investors. Section 206 of the Advisers Act *15 U.S.C. §80b-6*, makes it unlawful for any investment adviser - registered or not - "to engage in any transaction, practice, or course of business

which operates as a fraud or deceit upon any client or prospective client." *Id. §80b-6(2). In SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 84 S. Ct. 275, 11 L. Ed 2d 237 (1963),* [**24] the Supreme Court held that this provision created a fiduciary duty of loyalty between an adviser and his client. *See, id. at 191-92; id at 201.* ("The statute, in recognition of the adviser's fiduciary relationship to his clients, requires that his advice be disinterested."); *see also Hedge Fund Rule, 69 Fed. Reg. at 72,059 & n.57.* In that case, the duty of loyalty "requires advisers to manage their clients' portfolios in the best interest of clients," and imposes obligations to "fully disclose any material conflicts the adviser has with its clients, to seek best execution for client transactions, and to have a reasonable basis for client recommendations.

If the investors are owed a fiduciary duty and the entity is also owed a fiduciary duty, then the advisor will inevitably face conflicts of interest. Consider an investment adviser to a hedge fund that is about to go bankrupt. His advice to an investor in the fund, however, would likely include any and all measures to remain solvent. [**25] His advice to an investor in the fund, however, would likely be to sell.

> For the same reason, we do not ordinarily deem them the shareholders in a corporation the "clients" of the corporation's lawyer or accountants. *See RESTATEMENT, supra §96 cmt. B* ("By representing the organization, a lawyer does not thereby also form a client-lawyer relationship with all or any individuals...who have an ownership or other beneficial interest in it, such as its shareholders"). While the shareholders may benefit from the professionals' counsel indirectly, their individual interest easily can be drawn into conflict with the interest of the entity. It simply cannot be the case that investment advisers are the servants of two masters in this way.

Id. (Emphasis added.)

Contrary to the Appellate Court statement, Goldstein did not leave the issue of whether an investment adviser may simultaneously serve the client and the investor open. Goldstein explicitly eliminated that possibility.

In May of 2002, MDL founded the exempt ADF Hedge Fund in Bermuda. **Due to the nature of this investment vehicle and the rules and regulations related hereto, the ADF Hedge Fund was required to be established pursuant to a completely separate**

and distinct business relationship between MDL and the Bureau that was not connected to and in way dependent upon the pre-existing relationship with the Bureau. (Emphasis added). The ADF Hedge Fund consisted primarily of government, corporate, and mortgage-backed securities.

It is common knowledge now and at the time this fund was created that a hedge fund is a high risk investment vehicle. Concomitant with the potential for high gains is the risk of substantial losses, including the total loss of the investment. (PPM, p. 24). It is for this reason that a different set of rules and regulations apply to hedge funds. These rules and risks were fully described and outlined in the PPM, the documentation that governed the subject ADF Hedge Fund and that delineated the terms of the agreement between the Bureau, the ADF Hedge Fund, MDL and Mark Lay. By entering into the agreement, the Bureau accepted these terms and these risks. Pursuant to the agreement, the Bureau chose to accept the lack of fiduciary relationship and the risks and potential for a total loss of its investment due to unforeseen volatility of the market.

Several specific examples of this exist in the PPM. At the outset of the PPM, it is stated, in all capital letters:

> PROSPECTIVE SUBSCRIBERS IN THE FUND SHOULD INFORM THEMSELVES AS TO THE LEGAL REQUIREMENTS AND TAX CONSEQUENCES WITHIN THE COUNTRIES OF THEIR RESIDENCE AND DOMICILE FOR THE ACQUISITION, HOLDING OR DISPOSAL OF SHARES AND ANY FOREIGN EXCHANGE REGISTRATIONS WHICH MAY BE RELEVANT TO THEM. IF YOU ARE IN ANY DOUBT ABOUT THE CONTENTS OF THIS MEMORANDUM, YOU SHOULD CONSULT YOUR STOCKBROKER, SOLICITOR, ACCOUNTANT OR OTHER FINANCIAL ADVISER.

(PPM, p. ii).

The following excerpts from the PPM totally refute the claim that OBWC paid Petitioner's fee for work on ADF:

> **FEES AND EXPENSES**
>
> <u>Organization and Offering Expenses</u>
>
> The aggregate initial organization and offering expenses will be advanced by the

Investment Adviser and will be reimbursed by the Fund at such times and in such amounts as requested by the Investment Adviser. Provided that the Fund commences investing activities, the Fund may treat its organizational costs and expenses in accordance with U.S. Generally Accepted Accounting Principles, although it may elect to modify its treatment of such costs and expenses to accommodate its practical needs, including without limitation, by amortizing such organizational costs and expenses over a period of up to 60 months. Subsequent offering expenses will be direct expense of the Fund.

Investment Adviser Compensation

The Investment Adviser will receive a quarterly management fee determined at a rate equal to 1% per annum of the Fund's Net Asset Value, accrued monthly and payable in arrears as of the end of each calendar quarter. It also will receive a quarterly inventive fee (the "Incentive Fee") equal, in the aggregate, to 20% of the

increase in Net Asset Value of each series of Shares over the sum of (i) the Series' Net Asset Value as of the commencement of each calendar quarter plus (ii) the yield on the Fund's portfolio at a rate equal to the yield of the Lehman Government Credit Index for such period (the "Hurdle"). A series of Shares will only be charged with an Incentive Fee if its Net Asset Value at the end of a quarter (prior to accrued Incentive Fees), if any, for the quarter is greater that (i) its Net Asset Value at the time of its initial subscription (or the Initial Closing Date, whichever is later) or (ii) its Net Asset Value at the time the last Incentive Fee was charged against such Series, whichever is higher, plus the Hurdle (the "High Water Mark"). In the event that the Fund invests in the Master Fund, the Investment Adviser will not be entitled to a separate management or investment advisory fee as manager of the Master Fund but will be entitled to reimbursement for expenses incurred on behalf of the Master Fund.

In order to ensure that the Incentive Fee is charged only to Shares that have appreciated in value their acquisition and to make sure that all Shares have the same Net Asset Value, the Fund will issue different series of Shares to investors who invest at different times to ensure that the Incentive Fee is charged only to Shares that have appreciated in value. See "CHARGES TO THE FUND - Calculation of Investment Adviser Compensation."

Calculation of Investment Adviser Compensation

The management fee is accrued monthly in arrears and paid as of the end of each calendar quarter.

The Fund also will pay a quarterly Incentive Fee to the Investment Adviser equal to 20% of "Net Profit" with respect to each series of Shares. See "SERIES OF SHARES" below. "Net Profit" is defined as the excess of the Net Asset Value of a Series as of the end of the quarter (after deduction of the Management Fee accrued

for the quarter but excluding any deduction for Incentive Fees accrued on each Series) less the sum of (i) the Net Asset Value of the Series as of the first day of the quarter plus (ii) the amount of interest which would have been earned during the quarter if the Fund's net assets had been invested at a rate equal to the yield on the Lehman Government Credit Index for the quarter (the "Hurdle") adjusted to reflect subscription and redemptions with respect to such period.

Incentive Fees are based only on the portion of the appreciation in the Net Asset Value of a Series of Shares during a quarter that constitutes an increase in its Net Asset Value in excess of the sum of the cumulative Hurdle and its highest Net Asset Value as of the end of any prior quarter or, for the quarter the Series are redeemed at any time other than the end of a quarter, the date of redemption will be treated as such shares. The amount of any Incentive Fee accrued with respect to the redeemed Shares will be payable to the

Investment Adviser, notwithstanding that following the redemption, the Net Asset Value of the relevant Series of Shares decreases.

The Investment Adviser may, in its sole discretion, waive all or part of its Incentive Fee otherwise due with respect to any Shareholder's investment by rebate of the waived fees to such Shareholders. The Investment Adviser may also, in its sole discretion, elect prior to the commencement of the Fund's trading activities and prior to the commencement of each calendar year thereafter, to defer for a period of up to ten years all of any portion of the Management Fee or Incentive Fee to be earned with respect to such period. In the event of such deferral, the deferred amount will appreciate or depreciate, at the election of the Investment Adviser, based on either (1) the Fund's performance (before Management or Incentive Fees) or (2) the performance of any other investment chosen by the Investment Advisor prior to the commencement of the deferral period.

> The deferred fees will be reflected on the books of the Company as a liability and will reduce the Fund's Net Asset Value.

The language in the PPM makes it clear the Petition's fees were paid by Olympia Capital as Administrator for ADF, not OBWC. It also makes clear that whoever paid the fees had to have intimate knowledge of ADF's performance. Accordingly, it is inconsistent to contend that OBWC paid the fees but was misled concerning ADF status. In other words, it is illogical to contend that OBWC paid Petitioner's fees, but was not aware of factors such as the daily net asset value of ADF, a critical component of fee calculation.

OBWC was a sophisticated investor. Participation in ADF was limited to sophisticated investor.

In point of fact the PPM states:

> <u>Eligible Subscribers</u>
> The Shares are offered only to Qualified Holders. Qualified Holders are "non-United States Persons" and U.S. tax-exempt investors who are "qualified eligible participants" under CFTC Regulation 4.7 and "qualified purchasers"

under Section 3(c)(7) of the Investment Company Act.

Aside from errors related to fees, status as a client, the lack of gain and fraudulent mailings, the District Court erroneously failed to issue a proper instruction as required by United States v. Smith, 419 F.3d 521, 529 (6th Cir. 2005). Therein, the Sixth circuit stated that it is an abuse of discretion to fail to give a proper cautionary instruction "'to guard against the dangers of undue emphasis and context.'" Id. (quoting, United States v. Tines, 70 F.3d 891, 897 (6th Cir. 1995)). Smith emphasized the need to instruct as to both components, to prevent the undue influence on the jury regarding the testimony and to prevent taking the testimony out of context of the circumstances of the original testimony. Id.

During the jury deliberations, the jury requested to see the transcript of Mark Lay's prior testimony. Prior to allowing the jury's request, and over Appellant's objections, Judge Dowd of the District Court stated that he was only giving half of the instruction required by the Smith case because he did not understand the second requirement to caution the jury to not take the testimony out of context. (Trial tr., Doc. #145, pp. 552-554, October 30, 2007).

In this case it is reversible error that the full instruction was not given because the testimony the jury requested and received included Mark Lay's testimony when he was erroneously asked to give a legal conclusion. He was not qualified to give a legal conclusion, and that was error as well. (Trial tr. Doc. #145, pp. 552-554, October 30, 2007).

Failing to exclude or give a limiting instruction as to Mark Lay's opinions as to legal conclusions regarding client and investor was prejudicial to Mark Lay's defense, in and of itself. This prejudice was compounded by the district court's refusal to give the proper limiting instruction. The testimony was taken out or context by the jury. The jury was not told that Mr. Lay testified in civil case involving totally different issues.

CONCLUSION

By reason of these errors, Reconsideration should be accorded to Mr. Lay.

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